IN THE

Supreme Court of the United States.

No. 681. **October Term, 1924.**

C. G. LEWELLYN, Formerly Collector of United States Internal Revenue for the Twenty-third District of Pennsylvania,

Plaintiff-in-Error,

v.

ADELAIDE H. C. FRICK, HELEN C. FRICK, CHILDS FRICK, et al., etc.

In Error to the District Court of the United States For the Western District of Pennsylvania.

BRIEF OF AMICI CURIAE.

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ADELAIDE H. C. FRICK, HELEN C. FRICK, CHILDS FRICK, et al., Etc.

In Error to the District Court of the United States for the Western District of Pennsylvania.

BRIEF OF AMICI CURIÆ.

STATEMENT OF QUESTIONS INVOLVED.

(a) Is not a tax on the proceeds of a contract of life insurance payable to a beneficiary a direct tax?

(b) Has the Congress power to include, as a taxable part of a decedent's estate, the proceeds of life insurance policies payable to a beneficiary?

(c) Is not a tax on the proceeds of *any* life insurance policy, no matter to whom payable, a direct tax, save, perhaps, as to the withdrawal value of the policy, if any?

ARGUMENT.

The opinion of the Court below and the appellee's paper book have demonstrated, as to the very points involved, that the tax in question cannot be supported.

I. The act in question purports to lay an excise tax on the decedent's *parting with his estate at death.*

The tax, in general, is on the estate and is payable by the estate, not by the legatees, as in *Knowlton v. Moore*, 178 U. S. 41 (1900).

A tax on the proceeds of a life insurance contract cannot be a tax on an estate, because

(a) the contract was no part of the decedent's estate;

(b) the contract was *not parted with* at the time of death;

(c) the chose in action was transferred long before death.

II. The tax cannot be upheld as a tax on the right to receive the sum payable

(a) because that right became vested and perfect on the making of the contract; and

(b) because there is no privilege involved in the right to receive a gift.

III. Nor can it be upheld as a belated tax on the right to give, because

(a) such a right, being a natural right, is not subject to an excise tax; and because

(b) the right to dispose of property, by gift *inter vivos*, is one of the inherent attributes of property itself, and, hence, a tax thereon is a tax on property.

IV. The tax here is a direct tax upon a *chose in action; i. e.*, the right to receive a sum of money on the happening of an event.

V. The fact that such event is death, is an adventitious circumstance as respects

(a) the substance of the right;

(b) the ownership of the property;

(c) the character of the property; and

(d) its relation to the taxing power of Congress under the Constitution.

VI. A tax upon the *income* derived from property is a direct tax: *Pollock v. Farmers' Loan & Trust Co.*, 157 U. S. 429; 158 U. S. 601. *A fortiori* a tax upon the thing itself is a direct tax.

VII. A Lloyd's policy on the life of the King; a non-renewable term policy of insurance; an accident policy; an ordinary life policy, without surrender value; a policy containing a railroad-accident double-indemnity clause, illustrate the foregoing and show that **the payments finally accruing on such choses in action constitute new property,** coming into being synchronously with the phenomenon of inheritance, but governed by wholly different principles.

VIII. The fact that the duty to pay becomes effective at the moment of death is not determina-

tive because that duty existed *in posse* from the making of the contract and was the substance of the right acquired.

IX. The tax is void because not apportioned.

We submit the following analytical resume of the taxing power of Congress as applied to the proceeds of any life insurance policy:

I. Taxes are of two kinds:

1. Direct.

2. Indirect.

II. Limitations on Federal taxing power.

1. Direct taxes must be "in proportion to the census or enumeration herein before directed to be taken." (U. S. Constitution, Art. I, Sec. 9.)

2. Indirect taxes, such as "duties, imposts and excises shall be uniform throughout the United States." (U. S. Constitution, Art. I, Sec. 8.)

III. How distinguish between direct and indirect taxes?

1. Adopt the ingenious argument of Chase and Iredell, *JJ.*, in *Hylton v. U. S.*, 3 Dallas 171 (1796), that Congress can tax anything but exports, and, since direct taxes must be apportioned, any tax which can't conveniently be apportioned *must* be *indirect?* Scarcely!

2. The true rule is that the nature of the tax depends on the *nature* of the thing taxed.

3. If the tax is on a person or object, it is direct; if on the *privilege* of doing something, it is an excise and is indirect.

4. The borderline between a tax on an object and one on a privilege is sometimes hard to define. How find it? Examples are of aid.

5. What taxes are indirect? Examples:

(a) On the privilege of engaging in insurance business (measured by gross receipts). *Pacific Insurance Co. v. Soule*, 7 Wall. 433 (1868).

(b) On the privilege of State bank to issue banknotes for use as currency. *Veazie Bank v. Fenno*, 8 Wall. 533 (1869).

(c) On the right of succession (*i. e.*, right to leave real estate to person of decedent's choice). [Historically this is a right granted by the Crown, and never existed until so granted—it is not a *fundamental* right.] *Scholey v. Rew*, 23 Wall. 331 (1875).

(d) On the privilege of doing business at "exchanges"—a war tax. *Nichol v. Ames*, 173 U. S. 509 (1899).

(e) On the privilege of selling tobacco. *Patton v. Brady*, 184 U. S. 608 (1902).

(f) On the privilege of engaging in sugar refining business: *Spreckles Sugar Ref. Co. v. McClain*, 192 U. S. 397 (1904).

(g) On the privilege of receiving property by inheritance [Historically, same as (c) above]. *Knowlton v. Moore,* 178 U. S. 41 (1900).

(h) On the privilege of doing business in the form of a corporation. *Flint v. Stone Tracy Co.,* 220 U. S. 107 (1911).

6. Is *everything,* then, a privilege? Some of these seem farfetched. They fall, however, into two classes:

(a) Inheritance taxes 5 c and 5 g) [Historical basis above].

(b) Taxes on privilege of engaging in a particular business, or in business in a particular way. [From time immemorial, business has existed only on sufferance of the Crown, and subject to its regulation and interference.]

7. Are there no *rights,* as opposed to privileges? **Yes!** The *right* to receive the income on one's real *and personal* property: *Pollock v. Farmers' Loan & Trust Co.,* 157 U. S. 429, 158 U. S. 601 (1895). [Historically, this has always been a *right, not* a *privilege.*] Taxes on income are *direct.*

8. How about the *right* to give and receive gifts, *inter vivos?*

(a) Historically, this has always been recognized as a right, not a privilege—indeed, the Crown often took strong measures to induce them. (*Cf.* King John and the Jews.)

(b) Present gift tax clearly unconstitutional, at least, so far as it affects to hit genuine gifts *inter vivos.*

(c) Hence a tax on the right to give, and on the less blesséd right to receive, is *not* a tax on a privilege, but *is* a *direct* tax.

IV. Getting down to cases, just what is the nature of the relations arising when insurance is taken out? A (the insured) contracts with B (the insurance company). A agrees to make a certain payment, or payments, to B, in consideration whereof B agrees to make a certain payment to C (the beneficiary), on the happening of a specified event.

1. In *fire* insurance, C=A, and the event may never happen. Similarly in theft, etc., insurance.

2. In *accident* insurance, C=A, and the event may never happen.

3. In *life* insurance, the event *must* happen, and the promise becomes one to pay *at a time certain or ascertainable.*

(a) In *endowment* policies, C=A, and the promise is to pay at the end of a specified term of years.

(b) In *ordinary life* policies, C and A are distinct persons, and the promise is to pay when A dies.

(c) In policies taken out by persons having an *insurable interest* in the life of another, C=A, and the promise is to pay on the death of X, in whose life A has an insurable interest.

(d) In *wagering* policies, such as Lloyd's policies on the life of the King, C=A, and the promise is to pay when the King dies.

V. To resume, in a policy of life insurance, A contracts with B, agreeing to give B a particular sum of money in consideration for B's agreement to give to C a certain sum of money, at an ascertainable date.

1. How does this differ, in the essence, from the ordinary donee benficiary case, where A agrees to give B an elephant in consideration of B's giving C $1000 a year after delivery of the animal? (Donee beneficiary contracts recognized as enforceable in U. S. courts: *Nat'l Bank v. Grand Lodge,* 98 U. S. 123 (1878)]. It *does not differ.*

2. How does it differ—except in the *legality* of the transaction—from a bet, in which A and B agree that the survivor shall pay C $1000 on the death of the other? It *doesn't.*

3. Could Congress tax either of these? A tax on a gift *inter vivos* is a *direct* tax.

VI. Then, how can Congress tax insurance avails? The payment is from B (the insurance company) to C (the beneficiary), and can only be reached by a gift tax. Can it tax the proceeds of *endowment* policies, beyond, possibly under the income tax, as to the part thereof which is income?

VII. But, says Congress, let's call this an inheritance tax, because:

1. Avails of insurance on decedent's life are *part of the assets of the estate* of decedent. Are they? Then in IV-3-c above, the avails of insurance paid for by one having an insurable interest in decedent's life, become part of decedent's estate! Similarly, in IV-3-d, all those Lloyd's policies are part of the assets of the *King's* estate!! In any event, it is interesting to learn that a gift *from B to C*, is part of *A's* estate!!!

Well, then, perhaps it's because:

2. A paid the premiums. If he paid cash out, with no hope of getting it back, himself, that's the best kind of proof he hasn't got it, and nobody is inheriting it from him—*it isn't there to inherit.* Then, how about the donee beneficiary case (V-1)? A paid there, but there's no inheriting. Ah! it's because:

3. The property passes *as of the date of A's death.* Well, so it does:

(a) In the best case (V-2),

(b) In IV-3-c, the insurable interest case,

(c) In IV-3-d, where Lloyd's insure the King's life,

(d) *In all kinds of executory devises, and shifting and springing uses.*

In all these cases, the property passes as of the date of A's death, so, of course, somebody *must* be inheriting it *from him!*

VIII. Then, why *isn't* this an inheritance tax? Because:

1. It is on a contract whereby B, the insurance company) agrees to make a payment to C.

2. It is on something which wasn't decedent's property, so he couldn't give it, nor could anyone inherit it from him.

3. The beneficiary's right *vested* before decedent's death, which is merely the time when it takes effect in possession.

IX. What is this tax, then? It is a *direct* tax on either:

1. The right to make a gift; or

2. The right of the beneficiary to receive a gift.

X. Can it make any difference that the avails are payable to the executors or estate of A?

1. The general purpose of the Act of 1924 is not a tax on property, but a tax on the *cessation of interest of the deceased.*

2. It is not a tax on the right to such succession, since it is levied on the estate as a whole.

3. The power of Congress, therefore, is limited to taxing assets which in fact were in existence at the time of decedent's death and belonging to him.

If A, the decedent, had made a wager with B that A would die before B, and B paid the amount

of the wager to A's executor, would the sum be within the taxing power of Congress under the act? If it is said that the wager would not be enforceable, the answer is that there is no objection to the executor's receiving it, and if it were paid he would be obliged to account for it.

The essence of the situation is the same as in the case of insurance without insurable interest and waiver by the insurance company of the lack of insurable interest. Originally, wagers were enforceable; and even now an insurance contract is an enforceable wager.

A fatal accident results immediately on the taking out of an accident insurance policy, a policy having no cash surrender value; $10,000 is paid to the executor. It springs into being by reason of, not death, but death in a certain way. It is new property which has never belonged to the decedent.

A policy of insurance has a double-indemnity clause, increasing the amount payable in the event of death in a certain manner. Such death occurs. The same considerations apply.

4. **The fruit of the insurance contract is new property whose relation to the fact of death is contractual, not legal**; and this newly-arisen property becomes available by virtue of death in a particular manner, or by virtue of death in general.

5. The fact that insurance may be made payable to whomsoever the insured pleases, illustrates the character thereof. Insurance is a contract. It is a contract *inter vivos*. In general its perform-

ance turns upon the fact of death. It may turn upon the fact of death in a particular manner. Illustrations of assets which may come into the hands of executors, but which are beyond the taxing power of Congress in this regard are: Proceeds of an insurance policy where there is no insurable interest; a wager by A, the decedent, with B, that A would die before B and payment by B to A's executor; proceeds of an accident policy; proceeds of a double-indemnity clause increasing the amount payable in the event of death in a certain manner.

6. Regarded from the standpoint of a beneficiary other than the insured, the insurance money is a gift. The settled policy of all the income tax acts has been to regard gifts as not being income. The transaction of gift is now attempted to be taxed for the first time under the Act of 1924, as if it were the transmission of an asset by death. This tax is not an income tax, because it is levied on the giver—manifestly another illustration of a *direct tax on property,* the right to dispose of property being one of the three indispensable attributes of property and hence a tax thereon being a tax on property itself.

7. A tax upon the proceeds of an insurance policy is a tax levied upon *new property* which comes into being at the moment of decedent's death, but which is not the subject-matter of an inheritance tax or death duty because there has been no cessation of the interest of the decedent therein.

8. Cases in State courts permitting proceeds of insurance policies to be included are not controlling, because they depend upon the language of particular acts and varying constitutional restrictions. Where there is no constitutional obstacle and the tax is levied *upon all assets which are available for the payment of debts,* manifestly the tax is proper. On the other hand, if the insurance is payable to a beneficiary, it is not regarded as included in the estate at all. Thus in

> *Tyler v. Treasurer,* 115 N. E. 300 (See also Lawyers' Rep. Ann. 1907 D, p. 633),

the Supreme Judicial Court of Massachusetts held that

> ". . . proceeds of beneficial society certificates, payable to a deceased member's next of kin are not an estate or part of an estate, to be enjoyed after the death of a grantor or bargainor, and so are not subject to a collateral inheritance tax. . . ."

Again, in

> *Lord Advocate v. Fleming* (1897) A. C. (Eng.) 145, 66 L. J. P. C. N. S. 41, 76 L. T. N. S. 125, 45 Week, Rep. 674, 61 J. P. 692,

it was held that

> ". . . under the Succession Duty Act, which provides that 'every past or future disposition of property by reason whereof any person has or shall become beneficially entitled to any property or the income thereof upon the death of any person dying after the

time appointed for the commencement of this act either immediately or after any interval . . shall be deemed to have conferred a succession,' no part of the proceeds of a life insurance policy was liable to the tax where assured, several years before his death, gratuitously assigned the policy to his daughter, who thereafter paid the premiums."

9. It has been pointed out that tax laws should receive a practical consideration (*Knowlton v. Moore*, 178 U. S. 41 [1899]).

(a) The present situation as respects Federal and State taxation on the same subject-matter may be said to be one of emergency, if not of crisis.

Some of the States, including Pennsylvania, are taxing the entire nominal estate, including the vacuum created by the payment of tax to the Federal government.

The Congress, with greater decency, has permitted a deduction of taxes paid to the States in an amount not exceeding 25 per cent. of the Federal tax, thus furnishing a direct incentive to the States to increase their taxes to that amount.

It has been pointed out by President Coolidge that by reason of the taxability of property in different States and by the Federal government, there frequently arises something perilously near to confiscation. Each State attempts to tax all tangible property, disregarding the sound rule of common sense and common fairness that it follows the situs of the domicile of the owner, at any rate for the purposes of inheritance tax.

(b) Economists recognize that to take the principal of the savings of a lifetime and to divert

up to 40 per cent. thereof to the payment of current expenses of the Government, is for the community to live on its capital.

(c) Insurance is frequently taken out as a reserve, not merely for loss of productive power, but as against death duties. Whether policies are payable to the beneficiary, the wife or children, or the estate, the purpose is usually the same. To tax this reserve before it can be used for the purposes of paying taxes *is to penalize prudence.*

In non-liquid estates these enormous death duties result in possibilities of dislocation and disaster, and it is natural to provide a reserve by way of life insurance. The proceeds of insurance usually represent the results of self-denial on the part of the insured in his lifetime; the policy of the law should encourage adequate insurance protection.

10. The act refers to "insurance taken out by the decedent"—"taken out by" doubtless means "purchased by";—insurance on which the decedent has paid the premiums. This is confirmatory of the view that the tax is a tax on property and is regarded by the Congress as a tax on the property *of the insured*—for the result to the estate is precisely the same, whether someone else pays the premium or the decedent pays the premium.

11. We recur again to the main proposition that the proceeds of life insurance, whether payable to a beneficiary or to the insured, whether on an accident policy, a renewable term policy (having no surrender value), or a straight life policy, *constitute new property in respect of which there has*

been no cessation of interest on the part of the decedent. Such property comes into being at the moment of death and the tax on it is a direct tax and beyond the power of Congress.

In conclusion, it is submitted that the decree below should be affirmed—

(a) Because the tax in question was laid on property which did not belong to the decedent and which formed no part of his estate, either immediately before or immediately after his death.

(b) Because a tax on the proceeds of any contract of insurance is a tax upon property and hence a direct tax, requiring to be apportioned.

(c) Because Congress, while it may tax the cessation of interest of a decedent, cannot arbitrarily include in an inheritance tax law non-germane subject matters.

Respectfully submitted,

IRA JEWELL WILLIAMS, Jr.,
A. CARSON SIMPSON,
IRA JEWELL WILLIAMS,
FRANCIS SHUNK BROWN,
Amici Curiae.

Supreme Court of the United States

OCTOBER TERM, 1924.

No. 681.

C. G. LEWELLYN,
Plaintiff in Error,

v.

ADELAIDE H. C. FRICK ET ALS.,
Defendants in Error.

NOTICE.

Please take notice that the undersigned will submit to the Supreme Court of the United States on Monday, April 13, 1925, at Washington, D. C., at the opening of the Court on that day, or as soon thereafter as counsel can be heard, a motion for leave to file a brief in the above cause as *amicus curiae.* Copies of the motion and brief are hereto annexed.

WILLIAM R. SEARS,
Counsel for Hugh Bancroft, executor under the will of William A. Bancroft.

BOSTON, April 1, 1925.

941 Exchange Building,
Boston, Massachusetts.

Supreme Court of the United States

OCTOBER TERM, 1924.

No. 681.

C. G. LEWELLYN,
Plaintiff in Error,

v.

ADELAIDE H. C. FRICK ET ALS.,
Defendants in Error.

MOTION FOR LEAVE TO FILE BRIEF AS AMICUS CURIAE.

Now comes Hugh Bancroft, of Boston in the State of Massachusetts and a citizen of said State, and moves the Court for leave to file in the above entitled cause the brief herewith exhibited. Hugh Bancroft is executor of the estate of William A. Bancroft, his father, formerly a resident and citizen of Massachusetts, who died March 11, 1922, leaving a last will which has been duly admitted to probate.

William A. Bancroft during his lifetime had taken out policies of insurance upon his own life payable to beneficiaries other than the estate or the executor, namely, four policies payable to his wife, all dated

prior to 1903, in the total sum of $85,000, and two policies payable to his executors or administrators for the benefit of his then surviving children in equal shares, both dated prior to 1889, in the total sum of $15,000.

Upon the death of William A. Bancroft, Hugh Bancroft, having been appointed and qualified as executor, made return to the collector for the District of Massachusetts, setting forth among other information, as required by statute and regulations, the facts as to such policies, upon which return a tax was assessed under the Revenue Act of 1921, in the amount of $9,742.58, computed in part upon the excess of the amounts of said policies over $40,000. If the amount of said excess had not been included in the gross estate of the decedent, the amount of the tax would have been $2,408.09 less. The tax so assessed was paid by the executor on March 10, 1923, and a claim for refund of the amount of the tax assessed with respect to said insurance policies was filed at the same time.

HUGH BANCROFT,
Executor under the will of William A. Bancroft.

By WILLIAM R. SEARS,
Counsel.

Supreme Court of the United States

October Term, 1924.

No. 681.

C. G. LEWELLYN,

Plaintiff in Error,

v.

ADELAIDE H. C. FRICK et als.,

Defendants in Error.

BRIEF FOR HUGH BANCROFT AS AMICUS CURIAE.

STATEMENT.

This brief is filed in behalf of Hugh Bancroft, a resident and citizen of Massachusetts, executor of the estate of William A. Bancroft, who died March 11, 1922, a resident and citizen of Massachusetts.

William A. Bancroft during his lifetime had taken out policies of insurance upon his life payable in part to his wife and in part to his executors for the benefit of his then surviving children. The amount of these policies was $100,000. The rights of the beneficiaries under these policies had all accrued long prior to 1918.

An estate tax was assessed to Hugh Bancroft, as executor of the estate of William A. Bancroft, which was computed upon the value of the net estate, including the excess of the amounts of the policies referred to over $40,000. The tax so assessed was paid by the executor, and a claim for refund was made of the amount of the tax assessed with respect to said insurance policies.

The question in suit, in the decision of which the *amicus curiae* is directly interested, relates to the validity of estate taxes under the Revenue Act of 1918 (40 Stat. 1057, 1096, c. 18), re-enacted in the Revenue Act of 1921, so far as those taxes are laid upon or measured in part by "the excess over $40,000 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life."

THE STATUTE.

Pertinent provisions of the Revenue Act of 1918, imposing an estate tax on or measured by amounts receivable under life insurance policies are as follows:

Title IV. — Estate Tax.

. . . .

"Sec. 401. That . . . a tax equal to the sum of the following percentages of the value of the net estate (determined as provided in section 403) is hereby imposed upon the transfer of the net estate of every decedent dying after the passage of this Act, whether a resident or non-resident of the United States: . . ."

"Sec. 402. That the value of the gross estate of the decedent shall be determined by including the value at the time

of his death of all property, real or personal, tangible or intangible, wherever situated —

. . . .

"(*f*) To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life."

"Sec. 403. That for the purpose of the tax the value of the net estate shall be determined —

"(*a*) In the case of a resident, by deducting from the value of the gross estate —

. . . (Then follow certain deductions allowed by the statute, provisions in the case of a non-resident, etc.)"

"Sec. 407. That the executor shall pay the tax to the collector or deputy collector . . ."

"Sec. 408. . . . If any part of the gross estate consists of proceeds of policies of insurance upon the life of the decedent receivable by a beneficiary other than the executor, the executor shall be entitled to recover from such beneficiary such portion of the total tax paid as the proceeds, in excess of $40,000, of such policies bear to the net estate. If there is more than one such beneficiary the executor shall be entitled to recover from such beneficiaries in the same ratio."

ARGUMENT.

I.

The Tax Imposed by Title IV of the Revenue Act of 1918 is an Excise on the Transfer of a Decedent's Estate.

The nature of the federal estate tax has been fully explained and the power of the United States to lay

such a tax has been upheld in previous decisions of this Court.

> Knowlton *v.* Moore, 178 U. S. 41.
> New York Trust Company *v.* Eisner, 256 U. S. 345.
> Y. M. C. A. *v.* Davis, 264 U. S. 47, 50.

In the latter case the Court said regarding the estate tax imposed by the Revenue Act of 1918:

> "What was being imposed here was an excise upon the transfer of an estate upon death of the owner. It was not a tax upon succession and receipt of benefits under the law or the will. It was death duties as distinguished from a legacy or succession tax. What this law taxes is not the interest to which the legatees and devisees succeed on death, but the interest which ceased by reason of the death."

II.

Amounts Receivable by Beneficiaries Other than the Representatives of the Estate of a Decedent as Insurance under Policies taken out by the Decedent upon his Own Life are not Part of the Estate of the Decedent.

The general rule, it is submitted, is well settled that the interest of a beneficiary under a policy, whether that interest attaches by virtue of the policy itself or of a subsequent assignment (at any rate where no right is reserved to surrender or revoke the policy or to change beneficiaries), is a vested property right belonging to the beneficiary from the moment it is

acquired, of which the beneficiary cannot be deprived by any act of the insured either by deed or by will.

Central Bank of Washington *v.* Hume, 128 U. S. 195, 206.

"It is indeed the general rule that a policy, and the money to become due under it, belong, the moment it is issued, to the person or persons named in it as the beneficiary or beneficiaries, and that there is no power in the person procuring the insurance by any act of his, by deed or by will, to transfer to any other person the interest of the person named. . . .

"This must ordinarily be so where the contract is directly with the beneficiary; in respect to policies running to the person insured, but payable to another having a direct pecuniary interest in the life insured; and when the proceeds are made to inure by positive statutory provisions."

Mutual Benefit Life Ins. Co. *v.* Swett, 222 Fed. 200, 204.

"The rule is well settled that, under an ordinary policy of life insurance in which there is no reservation of a right to cut off or modify the interest of the beneficiary, the policy and the money to become due under it belong, from the time it issued, to the person named in it as the beneficiary, and that the insured is without power, whether by deed, assignment or will, or by surrender of the policy for a new one, or by any other act of his, to transfer to any other person the interest of the person so named as beneficiary. In such a policy the beneficiary acquires, the moment it is issued, a vested right which cannot be affected by any act of the insured subsequent to the execution of the policy, except it be a breach of condition. . . . If however, by the terms of the policy itself there is reserved to the insured the right, without the consent of the beneficiary, to change the appointee with the assent of the

insurer, the beneficiary acquires only an expectancy and not a vested interest during the life of the insured."

See also *In re* Simmons & Griffin, 255 Fed. 521.
Wilburn *v.* Wilburn, 83 Ind. 55.
Ricker *v.* Charter Oak Life Ins. Co., 27 Minn. 193.
Elliot's Appeal, 50 Pa. St. 75.
Anderson's Estate, 85 Pa. St. 202.
Entwistle *v.* Travelers Ins. Co., 202 Pa. St. 141.

This general rule obtains in Massachusetts.

Swan *v.* Snow, 11 Allen, 224.
Campbell *v.* New England Mutual Life Ins. Co., 98 Mass. 381, 400.
Gould *v.* Emerson, 99 Mass. 154.
Pingrey *v.* National Life Ins. Co., 144 Mass. 374, 382.
Haskell *v.* Equitable Life Ass. Soc., 181 Mass. 341.

Because the beneficiary and not the insured is generally speaking the owner of a life insurance policy and the one entitled to the proceeds thereof, it has been apparently consistently held that such property is not subject to legacy and succession taxes under state laws.

Tyler *v.* Treasurer and Receiver General, 226 Mass. 306.
Estate of Bullen, 143 Wis. 512, 523.
Matter of Parsons, 117 App. Div. (N. Y.) 321.

For these reasons, it is submitted, the amounts receivable by other beneficiaries as insurance under policies taken out by a decedent upon his own life ordinarily are not in fact part of the estate of the decedent.

III.

THE PROVISION IN SECTION 402 (*f*) OF THE REVENUE ACT OF 1918, INCLUDING IN THE ESTATE OF A DECEDENT SUBJECT TO TAX "THE EXCESS OVER $40,000 OF THE AMOUNT RECEIVABLE BY ALL OTHER BENEFICIARIES AS INSURANCE UNDER POLICIES TAKEN OUT BY THE DECEDENT UPON HIS OWN LIFE," IS UNCONSTITUTIONAL:

(A) *Because the Tax to the Executor, being laid on the Transfer of Property which is not a Part of the Decedent's Estate, is an Arbitrary Confiscation of the Property of the Estate in Violation of the Fifth Amendment.*

The tax imposed by Title IV of the Revenue Act of 1918 is in substance and effect a tax upon the transfer of that property the value of which enters into the computation of the tax.

The general principle has frequently been expressed by this Court that the constitutionality of a tax statute depends upon the substance rather than the form of the enactment. Thus in Postal Telegraph Cable Co. *v.* Adams, 155 U. S. 688, 698, the Court said:

"The substance and not the shadow determines the validity of the exercise of the power (of taxation)."

Again in Shaffer *v.* Carter, 252 U. S. 37, 55, it is said:

> "Where the question is whether a state taxing law contravenes rights secured by that instrument (the Federal Constitution), the decision must depend not upon any mere question of form, construction, or definition, but upon the practical operation and effect of the tax imposed."

See also Western Union Telegraph Co. *v.* Massachusetts, 125 U. S. 530.
Underwood Typewriter Co. *v.* Chamberlain, 254 U. S. 113, 120.

Moreover, the expressed purpose of the act itself is to tax the transfer of the same property whose value is the measure of the tax, for in section 401 it is provided that a tax equal to certain percentages of the value of the net estate is imposed upon the transfer of that same net estate.

The recent decision in Greiner *v.* Lewellyn, 258 U. S. 384, holding valid an estate tax under the Revenue Act of 1916 although nontaxable municipal bonds were included in the net estate, tends to support this construction of the act. There is no suggestion that the property which furnishes the measure of the tax may include anything other than the property whose transfer is taxed. The decision recognizes and assumes that the net estate whose transfer is taxed includes all the property in the gross estate referred to in section 402, less the deductions provided by section 403.

Clearly then, when the gross estate under section 402 includes an excess over $40,000 of amounts receivable by other beneficiaries under policies of insurance on the life of the decedent, and a tax is assessed

to the executor upon the transfer of the net estate calculated on the basis of that value, a tax is laid on the transfer of property which is not a part of the estate.

The question then is whether or not under the Constitution of the United States Congress in imposing a tax upon the devolution of property may provide arbitrarily that an estate shall be taxed for the transfer of property in which the decedent had no interest. More generally still the question is whether or not Congress can constitutionally impose a tax, either with respect to the ownership or the transfer of property, upon one who has no interest therein. Such a tax, it is submitted, is in violation of the Fifth Amendment in that it is a taking of a person's property without due process of law.

While the point seems never to have been directly decided there are several intimations of the Court to this effect.

In Hartman *v.* Greenhow, 102 U. S. 672, 684, the Court said:

> "And surely it is not necessary to argue that an act which requires the holder of one contract to pay the taxes levied upon another contract held by a stranger cannot be sustained. Such an act is not a legitimate exercise of the taxing power: it undertakes to impose upon one the burden which should fall, if at all, upon another."

In Knowlton *v.* Moore, 178 U. S. 41, 77, the Court said as follows:

> "It may be doubted by some, aside from express constitutional restrictions, whether the taxation by Congress of the property of one person, accompanied with an arbitrary pro-

vision that the rate of tax shall be fixed with reference to the sum of the property of another, thus bringing about the profound inequality which we have noticed, would not transcend the limitations arising from those fundamental conceptions of free government which underlie all constitutional systems. On this question, however, in any of its aspects, we do not even intimate an opinion, as no occasion for doing so exists. . . ."

In Flint *v.* Stone Tracy Co., 220 U. S. 107, 165–167, the Court, in holding the corporation tax law of 1909 to be constitutional, considered the contention that "measurement of the tax by the net income of the corporation or company received by it from all sources is not only unequal, but so arbitrary and baseless as to fall outside of the authority of the taxing power," and hence was void as lacking in due process of law. The Court disposed of the contention by showing that the measure was not arbitrary and baseless.

In Brushaber *v.* Union Pacific R.R., 240 U. S. 1, 24, 25, the Court said as follows:

"So far as the due process clause of the Fifth Amendment is relied upon, it suffices to say that there is no basis for such reliance since it is equally well settled that such clause is not a limitation upon the taxing power conferred upon Congress by the Constitution; in other words, that the Constitution does not conflict with itself by conferring upon the one hand a taxing power and taking the same power away on the other by the limitations of the due process clause. . . . And no change in the situation here would arise even if it be conceded, as we think it must be, that this doctrine would have no application in a case where although there was a seeming exercise of the taxing power, the act complained of was so arbitrary as to constrain to the conclusion that it was not the exertion of taxation but a confiscation of property, that is, a

taking of the same in violation of the Fifth Amendment, or, what is equivalent thereto, was so wanting in basis for classification as to produce such a gross and patent inequality as to inevitably lead to the same conclusion."

(B) *Because the Tax is in Fact on the Ownership and not on the Transfer of Property and is therefore a Direct Tax which is not Apportioned as the Constitution requires.*

An estate tax assessed to an executor under the Revenue Act of 1918, the amount of which is enhanced by including in the measure amounts receivable under insurance policies by beneficiaries other than the decedent, is a tax assessed in part on something other than a transfer of the estate of the decedent. It is a tax, therefore, which in part is not an estate tax at all. Apparently Congress has recognized this fact by providing in section 408 that the executor may recover that portion of the tax from the beneficiaries. The rights represented by such policies, as we have seen, are property rights belonging to the beneficiaries. Payment to the beneficiaries is merely a performance of the contracts of insurance. It is these property rights and not a transfer of anything which Congress has attempted to tax. It follows that the tax so far as it is assessed with respect to such policies is not an excise but a direct tax which must be apportioned.

Pollock *v.* Farmers' Loan & Trust Co., 157 U. S. 429, 583; 158 U. S. 601, 618, 630, 637.
Knowlton *v.* Moore, 178 U. S. 41, 78–83.
New York Trust Co. *v.* Eisner, 256 U. S. 345.

IV.

THE ACT DOES NOT APPLY TO AMOUNTS RECEIVABLE BY BENEFICIARIES UNDER POLICIES TAKEN OUT IN THEIR NAMES OR ASSIGNED TO THEM BEFORE THE PASSAGE OF THE ACT.

The policies which are the basis for the claim in suit, and also the policies with respect to which the *amicus curiae* has claimed a refund, were all taken out and the rights of the beneficiaries thereunder were all established before the passage of the Revenue Act of 1918. It is submitted that this statute is not to be construed retroactively as affecting those rights.

The principle involved seems to be clearly established by the recent case of Shwab *v.* Doyle, 258 U. S. 529. There a transfer by deed, in trust to pay the net income for life to the decedent and after his death to his children, executed by the decedent before the passage of the Estate Tax Act of 1916, was held not to be subject to the provisions of that act by which a tax was imposed on the transfer of the net estate of every decedent dying after the passage of the act, to the extent, among other provisions, of any transfer by the decedent at any time in contemplation of death. The Court was of the opinion that both principle and authority required that the act should not be construed to apply to transactions completed when the act became a law.

This principle, it is submitted, governing transfers in contemplation of death should be equally applicable to cases arising under section 402 (*f*) of the Revenue

Act of 1918, and should lead to the inevitable conclusion that the act must be construed not to apply to transactions by which life insurance policies were taken out in the name of or assigned to other beneficiaries than the decedent, so that the rights of those beneficiaries became fixed, at a time previous to the passage of that act.

Respectfully submitted,

WILLIAM R. SEARS,
ALEXANDER LINCOLN,
Counsel for Amicus Curiae.

Supreme Court of the United States

October Term, [illegible]

No. [illegible]

C. G. LEWELLYN, Formerly Collector of United States Internal Revenue for the 23rd District of State of Pennsylvania,

Plaintiff in Error,

vs.

ADELAIDE H. C. FRICK, HELEN C. FRICK, CHILDS FRICK, A. C. McELDOWNEY and WILLIAM WATSON SMITH, Executors of the last will of Henry C. Frick, deceased,

Defendants in Error.

IN ERROR TO THE DISTRICT COURT OF THE UNITED STATES FOR THE WESTERN DISTRICT OF PENNSYLVANIA.

BRIEF OF TYSON S. DINES, PETER H. HOLME, HAROLD D. ROBERTS AND CHARLES E. WORKS, AMICI CURIAE, ON BEHALF OF MARY DEAN REED, AS EXECUTRIX OF THE LAST WILL AND TESTAMENT OF VERNER ZEVOLA REED, Deceased.

Tyson S. Dines,
Peter H. Holme,
Harold D. Roberts,
Charles E. Works,
Amici Curiae.
First National Bank Building,
Denver, Colorado.

[illegible]

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TABLE OF CASES.

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Tyson S. Dines, Peter H. Holme, Harold D. Roberts and Charles E. Works, with consent of counsel for the parties above named, and after first having asked and obtained leave of Court, file this brief herein and to show grounds for their especial interest in the case at bar state the following facts:

STATEMENT.

The writers of this brief represent Mary Dean Reed as sole executrix of the last will and testament of Verner Zevola Reed, her deceased husband, in a suit now pending on demurrer in the Federal District Court for the District of Colorado and entitled *Reed v. Howbert.* By this suit Mrs. Reed seeks to recover from Howbert, United States Collector of Internal Revenue, the sum of approximately one million dollars, paid under protest as an additional estate tax levied under the Federal Estate Tax Law of 1918, in respect to the property in a *trust created in 1902.* Mr. Reed *died April 20, 1919*—a few months after the passage of the law.

The trust was irrevocable and provided for the payment of the income to the decedent for life with remainders to his descendants. The value of the property actually and absolutely transferred to the trust was at the time of transfer approximately two and a quarter million dollars. The value of the assets in the trust at the date of death and assessed as of that date, was about four million dollars. Thus an incremented capital value of approximately one and three-quarter million dollars accruing to the corpus after its transfer to the trust and never owned or transferred by the donor of the trust, was taxed as part of the decedent's estate. Furthermore, over a half million dollars worth of the assets in the trust at date of death were substitute assets resulting from reinvestments by the trustee. These had never been owned or transferred by the donor, but were taxed as a part of the estate.

By a demurrer to the Government's answer, plaintiff has raised the question of the constitutionality of the retroactive provisions of Section 402 (c) of the Revenue Act of 1918 when applied to gifts made years prior to its enactment. The Government's answer presents the theory that these gifts were transfers intended to take effect in possession or in enjoyment at or after death.

The retroactive taxation of a transfer intended to take effect at death is, in respect to its constitutionality, similar to the retroactive taxation of life insurance. In the Reed case, rights were created through transfers to a trustee; in the Frick case, rights were created through the making of life insurance contracts. In both cases the rights were created prior to the passage of the Estate Tax Law. Although there are differences in the nature of the two transactions, these differences are not material in the questions here to be discussed, as the general effect and result of the tax in both cases are similar.

We are satisfied that when a matter of such general importance as the validity of the retroactive features of the Federal estate tax is before the Court, it is or may be of assistance to the Court that it have presented at one time as many different angles and effects of the law as possible. This was obviously true in the *Shwab v. Doyle* group of cases. The Court's judgment in the case at bar while narrowly concerned with the insurance provisions of Section 402 of the Act, may possibly deal with the broad question of the validity of the expressly retroactive provisions of that Section. The Reed case directly and necessarily raising the question as to the constitutionality of those retroactive provisions, should, we believe, be brought to the attention of this Court now, even though it be far in advance of the time when it may normally come here for decision.

In the following pages we shall argue as briefly as may be, that the retroactive provisions of the Federal Estate Tax Law of 1918, whether applied to an irrevocable trust created before the law was enacted as in the Reed case, or applied to preexisting life insurance policies as in the Frick case, in their essence impose a tax on a past transaction—on a completed transfer. We shall then discuss and attempt to dispose of some other and, as we believe, fallacious

theories as to the true nature of the tax. Then we shall proceed to show that these provisions when properly analyzed impose a tax unconstitutional, first as an unapportioned direct tax; second, as a deprivation of property without due process of law and a taking of private property without just compensation; and third, as a violation of the fundamental conceptions of free government.

ARGUMENT.

I.

THE NATURE OF THE FEDERAL ESTATE TAX ACT OF 1918 AS APPLIED TO TRANSACTIONS COMPLETED BEFORE THE LAW WAS ENACTED.

A.

IN ITS ESSENCE IT IS A TAX UPON A PAST TRANSACTION — A TAX UPON A COMPLETED TRANSFER.

The Revenue Act of 1918 provides in part as follows:

> "Sec. 401. That * * * *a tax* equal to the sum of the following percentages of the value of the net estate (determined as provided in Section 403) *is hereby imposed upon the transfer of the net estate* of every decedent dying after the passage of this Act * * *."
>
> "Sec. 402. That the value of the gross estate of the decendent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated * * * *;"
>
> "(c) To the extent of any interest therein of which the decedent has at any time *made a transfer*, or with respect to which he has at any time *created a trust*, in contemplation of or intended to take effect in possession or enjoyment at or after his death (*whether such transfer or trust is made or created before or after the passage of this act*), * * *.
>
> "(f) To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent

of the excess over $40,000.00 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life."

"Sec. 407. That the Executor shall pay the tax to the Collector * * *."

That if there is an unpaid excess "Such excess shall be *a lien upon the entire gross estate* * * *."

"Sec. 408. * * * If any part of the gross estate consists of proceeds of policies of insurance upon the life of the decedent receivable by a beneficiary other than the executor, the executor shall be entitled to recover from such beneficiary such portion of the total tax paid as the proceeds, in excess of $40,000.00 of such policies bear to the net estate."

"Sec. 409. That unless the tax is sooner paid in full, it shall be a *lien* for ten years *upon the gross estate* of the decedent * * *."

"If (a) the decedent *makes a transfer* of, or *creates a trust* with respect to, any property in contemplation of or intended to take effect in possession or enjoyment at or after his death (except in the case of a bona fide sale for a fair consideration in money or money's worth) or (b) if insurance passes under a contract executed by the decedent in favor of a specific beneficiary, and if in either case *the tax in respect thereto* is not paid when due, then the tranferee, trustee, or beneficiary shall be personally liable for such tax, and such property, to the extent of the decedent's interest therein *at the time of such transfer,* or to the extent of such beneficiary's interest under such contract of insurance, shall be subject to a like lien equal to the amount of such tax * * *." (Italics ours.)

The ultimate, the essential nature of the retroactive provisions of this tax, rather than the name by which the

statute in its entirety goes, is the first important matter to be determined. This essential nature is to be ascertained by looking to the substance of the Act and to the effect of the Act when these retroactive features are applied to the transactions of the persons claimed to be within its scope. We believe that this Act retroactively applied is neither an estate tax, an inheritance tax, nor a death duty of any kind. It is either a tax on certain persons because they transferred property or created rights prior to the passage of the law, or a tax on past transactions. In either case it is a direct tax.

> Congress said: *"A tax is hereby imposed upon the transfer of the net estate"* etc.

This is not a tax upon the *receipt* of anything by anybody. Congress did not approach the problem from the viewpoint of the recipient. The law looks at the entire property of a man about to die and it says: Before you can finally pass on any interest in what is yours at the moment of death (or in some instances in what used to be yours), the Government must first be satisfied.

The thing sought to be taxed, "the net estate", is no isolated phrase shorn of a context, neither is it a theoretical or algebraic concept or other mathematical abstraction. It is always a direct derivative of the gross estate and what constitutes the gross estate the law makes clear, as well as what may be deducted therefrom. Every item that goes into the gross estate directly swells the resultant net estate. Congress did not intend to enforce a tax on a man's obligations, on the expense involved in the machinery of winding up his affairs after death. It did not see fit to tax the first $50,000.00, nor to tax property that had recently paid a government estate tax, nor to tax his public or charitable gifts. It therefore allowed certain deductions (Sec. 403).

Nevertheless, Congress included all his property in its definition of his gross estate, the value of which, item by

item, the executor's report must state. Furthermore, when it dealt with the subject of payment of the tax, and was making sure that the Government should be protected, it did not limit the Government's lien to the net estate; it provided that the lien should be "upon the entire gross estate" (Sec. 407) or "upon the gross estate" (Sec. 409). So when the statute is read as a whole, as of course it must be, the thing obviously sought to be taxed and actually taxed is the passage or the transfer of property—call it the transfer of a value, or the transfer of the net estate, or what you will—*it is the transfer of property*, the thing of value that human beings are all seeking to get. That this is a tax on the transfer of the decedent's estate and primarily collectible from his estate as a whole seems obvious.

Now apply this law, this tax upon the transfer of the net estate, to the facts of the Reed case. In 1902, sixteen years before the passage of the 1918 Estate tax law, Reed creates a trust; he puts certain property absolutely out of himself and into the trustee; he reserves no power to recall it; the transaction is complete; he has finally parted with title. When he makes these gifts he is doing a legitimate thing. He is not evading. There is no occasion for the existence of an ulterior motive. The 1918 law is passed a few months before he dies. It taxes his precedent transfers of these assets and makes his estate pay not 25% of their value when he parted with them—that would have been bad enough—but 25% of the value of everything in the Trust into which they had grown on the date of death.

Years before the 1918 law, Mr. Frick takes out life insurance policies and makes them run irrevocably in favor of his wife and his daughter. These were perfectly legitimate acts; no evasion was present. Then the 1918 law comes into being and taxes his past act of taking out life insurance policies and collects the tax from his Executor and from the beneficiaries through an imposition based, not on the aggregate value of the money he had parted with in pre-

miums, but on the values into which the policies had grown at the time of his death.

In each case values are taxed which never at any time had been the decedent's; assets which at no time had belonged to him.

Therefore, when we look, not to the name by which this whole tax law is called, but to the essential nature of the retroactive clauses when applied to transactions such as these, what can this law be but a tax on past transfer of property, a past transaction, a completed gift?

Certain of the provisions of the law under discussion were borrowed from State inheritance tax laws which have been unanimously construed as taxing the original transfer. In *Keeney v. New York*, 222 U. S. 525, this Court held valid a New York tax on a transfer, intended to take effect at death, of personal property of a non-resident, although the property was no longer in New York at the date of death. This Court expressly held the tax to be on the original transfer, saying at page 537:

> "The validity of that burden must be determined by the situation as it existed in 1903, *when the deed was made.*" (Italics ours.)

Both in the case of transfers in contemplation of death and in the case of transfers intended to take effect in possession or enjoyment at or after death, the original transfer is the only transfer from or by the decedent, and is unquestionably the transfer sought to be taxed by the Act. In seeking to reach the life insurance of a decedent, Congress must have grounded the tax on some act for which the decedent was responsible; either the payment of premiums, or the naming of a beneficiary.

In defending the numerous suits brought by taxpayers to recover taxes assessed under the 1916 estate tax law, as well as under the 1918 law, counsel for the Government have

resorted to various theories as to the real nature of these statutes. It is obvious in their statement of these theories that they have sought to avoid the admission that either of these statutes was retroactive in the full sense, the brazen sense of the word. They have tried to show that even though reaching back into the past, there was still some act, some occurrence in the instant case, taking place subsequently to the enactment, that would give the law a prospective operation. This is a commendable attitude on the part of Counsel, for it is inherently offensive to any right thinking person, to any lover of fair play, to hold a man to the consequences of his act when the consequences were unforeseeable and came into being as consequences only because of the later enactment of a law.

While we believe there is but one tenable theory as to the nature of this tax retroactively applied, namely that it is *a tax on a past completed transfer*, nevertheless, before proceeding to a discussion of the constitutional questions, we feel it desirable briefly to consider certain other theories which, from time to time, have been advanced and which we deem unsound. Thus we hope to leave unquestionable our premise as to the true nature of the tax.

B.

THE COMING INTO POSSESSION THEORY OF THE NATURE OF THE TAX.

According to this theory the Government asserts that this is not a tax on a past transfer, but a tax on the present privilege of coming into possession, and hence that the act does not really affect past transactions. Stated somewhat differently, the theory is that the tax is on the right of the remaindermen to come into possession of their remainders, or of the insurance beneficiaries to receive the proceeds of their policies.

The answer to this theory is manifold. First, the law expressly purports to be a tax on a transfer, not on the privilege of receiving.

Second, the decision of the courts show that it is a tax upon a transfer.

In *Curley v. Tait,* 276 Fed. 840 at page 844, the Court said in a case involving the 1916 law:

> "The present act, unlike its federal predecessor, is an estate tax, and *not a tax upon the right to receive.* If the Government's contention be sustained, the tax will come, not as in *Wright v. Blakeslee, supra,* or in *Cahen v. Brewster,* 203 U. S. 543 * * * out of the sum received by the one to whom the taxed property passes, but will be collected from one to whom it does not." (Italics ours.)

This Court in *Shwab v. Doyle,* 258 U. S. 529, must have deemed the 1916 law to impose a tax on the transfer because by denying it a retroactive effect it held that it could not reach the past transfer. If this Court had regarded it as a tax upon the coming into possession it would have reached a contrary conclusion as to the taxpayer's right to recover in that case.

Again in *Edwards v. Slocum,* 264 U. S. 61, decided in January of 1924, this Court through Mr. Justice Holmes said at page 62 in speaking of this estate tax law of 1918:

> "But this is not a tax upon a residue; it is *a tax upon a transfer* of his net estate by a decedent, a distinction marked by the words that we have quoted from the statute, and previously commented upon at length in *Knowlton v. Moore,* * * *. It comes into existence before, and is independent of, the receipt of the property by the legatee" (italics ours).

See also *Y. M. C. A. v. Davis,* 264 U. S. 47.

A third phase of the answer to the coming into possession theory is that it is inconsistent with the taxing of transfers in contemplation of death, as well as of gifts to take effect in possession *after* death. In the same sentence of paragraph (c) of Section 402, gifts in contemplation of death as well as gifts intended to take effect in possession or enjoyment *at* or *after* death, are dealt with and so dealt with as to be placed on a parity.

If a man expressly makes a gift in contemplation of death a week before he dies, there is no coming into possession when he dies—that occurrence has already taken place, and if the law does not tax the transfer, there is nothing for it to tax. Furthermore, the tax could be successfully evaded today if expressly in contemplation of death a man parted with all of his property just before he died. No one would come into possession at or after his death and no tax would be assessable. Suppose an estate consisted of only two items: One a gift in contemplation of death, the other of equal value, being a gift to take effect at death. We submit that it would be utterly at variance with the structure of this statute to select the first item and say as to it that the tax was on the transfer, but as to the second item it was a tax on the coming into possession. This would be to adopt two different theories as to the nature of the tax according as it were to be applied to one or the other of two types of gift embraced in the same sentence of the statute and obviously treated alike.

In reporting on the Federal Estate Tax of 1916 the committee on Ways and Means said (Report No. 922, 64th Congress, First Session):

> "Your Committee deemed it advisable to recommend a Federal Estate Tax upon the transfer of the net estate rather than upon the shares passing to heirs and distributees or devisees and legatees."

In addition to all these reasons for holding the tax to be in its nature a tax upon the transfer and not upon the coming into possession, we suggest that the very method of taxation under which the estate, rather than the legatee or remainderman, pays the tax is more than significant. The rate of the tax and its amount are based not on what is received, but on what is transmitted. Even in the case of transfers intended to take effect at or after death, or transfers made in contemplation of death, the burden of the tax falls, not upon the transferee, but upon the residuary estate (except where the assets of the estate are not sufficient to pay the tax).

> *Farmers Loan & Trust Co., v. Winthrop*, 238 N. Y. 488; certiorari denied, 45 Sup. Ct. 225.
> *Bemis v. Converse*, 246 Mass. 131;
> *Pratt v. Dean*, 246 Mass. 300.

The date of coming into possession does not necessarily fix or have any relation to the date of paying the tax. If the decedent has made a gift to take effect twenty years *after* his death, the tax will be payable at his death, or twenty years before there is any coming into possession. If the property be lost, stolen or destroyed in the interval the donee never will come into possession.

Even if this could be construed to be a tax on the right to come into possession of a remainder, or the right to take possession of the proceeds of an insurance policy, where the property rights are already vested in those taking possession, the tax would be a direct tax and unconstitutional because not apportioned, as argued elsewhere in this brief.

> *Dawson v. Kentucky Distilleries*, 255 U. S. 288.
> *Matter of Pell*, 60 N. Y. App. Div. 286; affirmed 171 N. Y. 48.
> *Craig v. Taylor & Sons*, 192 Ky. 36.
> *Thompson v. Kreutzer*, 112 Miss. 165.
> *Thompson v. McLeod*, 112 Miss. 383.

C.

THE UNCOMPLETED TRANSFER THEORY OF THE NATURE OF THE TAX.

According to this theory, transactions such as took place in 1902 in the Frick and in the Reed cases are sought to be viewed as not really complete until death made them so; and that as this event occurred after the law was passed the law is not truly retroactive.

One fatal defect in this theory is that it fails to cover the case of gifts in contemplation of death, and is absolutely inconsistent with the attempt to tax them. Suppose Reed had made a gift which on its face had carried evidence conclusive of its being of that character. His death could have had no possible bearing on the situation except to fix the date on which the tax was payable. Again two distinct theories of the tax would have to be resorted to in applying Sec. 402 (c) according as the Department might be dealing with one sort of gift or the other.

When the property was transferred to the trust in 1902, the owner had performed his last act in respect to it and nothing he could say or do thereafter could change what he had done. It is true the date of full possession and enjoyment on the part of his children was postponed until his death; but to press that point forces the government back into the coming into possession theory already discussed. So far as Mr. Reed's rights were concerned, the transfer was irrevocable, indefeasible and complete and its terms were fixed when it was made. It must always be borne in mind that the whole scheme of this law was developed from the end of the transaction opposite to that which forms the basis of the usual state inheritance tax laws. It is the "whence" rather than the "whither" which must be considered.

In holding unconstitutional a similar law, the New York Court said in re *Webber,* 151 N. Y. App. Div. 539 at 541:

> "The deed became operative immediately upon its delivery with the intention of vesting title in the trustees for the purposes of the trust, which provided for the final distribution of the property, and only the benefits were postponed to the happening of a particular event, and the law of that contract must be determined by the law as it existed when the deed became effective."

This uncompleted transfer theory is obviously but another effort to get away from the obnoxious retroactive tax—it is an effort to fasten upon something occurring *after* the passage of the law as the basis for the imposition.

D.

THE MEASUREMENT THEORY OF THE NATURE OF THE TAX.

This theory may be stated in several ways, but all are variations on the same theme. From the contentions of the Government in a case decided on Jan. 28, 1925, by the Federal District Court of Massachusetts, entitled *Coolidge et al. v. Nichols* (not yet reported), it would seem that some form of the measurement theory is what the Government has finally adopted as its defensive argument.

One possible statement of this theory is that past transfers *inter vivos* may properly be included in the computation of the tax as a measure of the tax even though the thing taxed is only the transfer of property owned at the time of death.

This theory would permit, without taxation, the transfer of an entire estate in contemplation of death; because, while the measure would exist, the matter to be taxed, i. e., the transfer of *things owned at death,* would not. No tax could

be collected in those cases where the decedent dies without leaving any estate, as in *Levy v. Wardell*, 258 U. S. 542. Congress certainly never intended any such result as that.

Furthermore, this theory would here result in a tax on A's property measured by the value of B's property and thus fall within the inhibition recognized in *Knowlton v. Moore*, 178 U. S. 41, and so conclusively illustrated in the hypothetical case set out by Mr. Justice White at page 76 (quoted *infra*, page 43).

Another statement of the same theory is that the "net estate", the *value* of which determines or measures the tax, includes everything taxable under the act; but that the "net estate", the *transfer* of which is taxed, includes only property which was actually possessed by decedent at his death.

Sec. 401 of the Act provides:

> "A tax equal to the sum of the following percentages of the value of the *net estate* (determined as provided in Section 403) is hereby imposed upon the transfer of the *net estate* of every decedent" * * *. (Italics ours.)

In other words, this theory requires that the phrase "net estate" shall have two different meanings in the same section and sentence of the law; that "net estate", as it first appears in Section 401, and the *value* of which is to measure the tax, shall be different from "net estate", used in the next line of the same sentence, the *transfer* of which is taxed. There is no ground for believing that Congress intended different meanings for these two identical phrases. Under the well settled rule of construction they should be given the same meaning.

The scheme of the Act inherently shows that the past transfers themselves are taxed and that they do not serve merely as the measure of a tax on something else. As indicated earlier in this argument the tax in certain events may be collected from the transferee or trustee per-

sonally or out of the actual property transferred. See Sec. 409. Neither one of these possibilities is consistent with the theory that the past transfers are merely measuring rods. They are the substance, not the shadow.

Sec. 409 provides:

> "If (a) the decedent makes a transfer of, or creates a trust with respect to any property in contemplation of or intended to take effect in possession or enjoyment at or after his death * * * and if in either case *the tax in respect thereto* is not paid when due then the transferee * * * shall be personally liable," etc. (Italics ours.)

The measurement theory would make these words meaningless. The tax is on and in respect to these transfers as definitely as words can place it there.

The Government in its brief in the *Coolidge* case, (*supra*) stated that this tax "is imposed not upon a transfer of property but upon the transfer of the 'net estate' which under the statutory definition is not property, but is merely a value", and that "The tax is measured not by the *transfer* of property but by the *value of property.*" This sounds like a play on words.

In the Reed case the Executrix reported on all the property of the testator, but excluded that covered by this trust. The usual deductions were subtracted and the tax paid on the net estate. Later the Commissioner valued the assets of the trust as of the date of death and collected a tax of 25% on the total valuation. The amount of the tax in dispute was imposed upon, and arose solely from the value of these trust assets included as a part of decedent's net estate. Call this additional tax what you may; a tax on the net estate, a tax on "a value", a tax on an occasion, a tax on the "cessation of an interest"—the fact is that all of the assets included in the past gift were appraised and 25% of that appraised value had to be paid

by the Executrix and if she had had nothing with which to pay it, the trustee and the beneficiaries would have been held personally liable for it.

Counsel for the Government in some of these cases have contended that this is "*a tax on a present occasion* measured by some past event"; "a tax generated by the decedent's death."

If Congress intended this to be a tax on a "present occasion", viz., a tax *on death*, why did Congress use the expression "A tax * * * is hereby imposed *upon the transfer of the net estate* of every decedent dying after the passage of this Act"? How could language be more aptly chosen to express the intent to tax the *transfer of property?* This is not a tax on the privilege or the fact of dying measured by the decedent's past life and conduct. If Congress had meant that, it could easily have said so. The resort to a fanciful, hairsplitting, contrary-to-fact argument carries with it its own refutation.

Even if the law could be construed in accordance with the measurement theory, it would be unconstitutional. No amount of subtle reasoning can obscure the plain fact that this is in truth a tax in respect to the life insurance or to a past gift and not merely a tax on something else but measured thereby. It is well settled that a valid excise tax on one thing cannot be measured by the value of some other thing which cannot be taxed. *Knowlton v. Moore, supra; Wallace v. Hines,* 253 U. S. 66; *Delaware L. & W. Ry. Co. v. Pennsylvania,* 198 U. S. 341; *Galveston, Harrisburg, etc., Ry. Co. v. Texas,* 210 U. S. 217; *Western Union Telegraph Company v. Kansas,* 216 U. S. 1.

Our position is not in conflict with *Flint v. Stone Tracy Co.,* 220 U. S. 107. There the tax was expressly upon the privilege of doing business, not upon income. The privilege was measured by the income of the corporation. This was upheld even though a part of such income would have

been exempt from ordinary taxation. The decision was rested expressly on the ground that this was in substance, as well as form, a tax not on the income, but on the true value of the privilege of doing business. The total income, including that from exempt sources was held a true and reasonable measure of the value of the privilege taxed. In *Maxwell v. Bugbee,* 250 U. S. 525, the New Jersey Inheritance Tax Law was upheld even though the rate of tax was made to depend upon all of the property of the decedent whether within the taxing jurisdiction of the state or not. Extraterritorial, nontaxable property was not *taxed* in that case, although the *rate* of tax in New Jersey was fixed by a wholly reasonable standard which incidentally included nontaxable property. But even the property considered in determining the rate of tax was property all belonging to the decedent at his death, and there was no intimation that property *previously disposed of* and belonging to another person could be considered for any purpose.

According to the measurement theory, the tax in the present case is a tax on A's estate measured by B's property. In other words, it is a tax on B's property collected from A. There is absolutely no authority even suggesting that such an exaction would be valid.

E.

THEORIES THAT THE TAX IS ON THE PASSING OF PROPERTY AT DEATH OR ON THE CESSATION OF AN INTEREST.

In endeavoring to arrive at the true nature of this tax—what it really is—as applied to the facts of the Frick or Reed case, it may be helpful to point out one or two more things which it is not. When retroactively applied, *it is not a tax upon the passing of property at or after death.* In the case of the gifts to the trust prior to 1916, the property did not pass from the decedent on his death. Upon the transfer made irrevocably several years before,

the property had ceased to be Reed's. When he died no title passed from him. What the beneficiaries got was not his life estate, nor his property. Long before Mr. Reed's death his children had the ownership in this property, subject to his life estate, and when he died and his life estate ended, they merely came into the enjoyment of their own property.

Hunt v. Wicht, 174 Calif. 205, involved a transfer to take effect at death. In holding unconstitutional a subsequent tax on the transfer the Court said (p. 209):

> "The succession to the property by the grantee * * * was complete upon the delivery of the deed in escrow, notwithstanding the reservation of the life estate * * * His death added nothing to the title theretofore acquired by the grantee, and there was no transfer of any property in any legal sense at the time of such death * * *."

See In Re *Webber*, 151 N. Y. App. Div. 539, *supra*.

The impropriety of holding that this law taxes any succession at death is apparent if we consider what would have been the case if in 1902 Reed had made an absolute *gift in contemplation of death*. Both the title and possession and enjoyment would have passed at once; at his death absolutely nothing would have happened and yet under the 1918 law a tax would have been levied. We submit this clearly shows that the tax cannot be a tax on the passing of property at death. If no property passes there is nothing on which to levy a tax.

In *Knowlton v. Moore*, 178 U. S. page 78, speaking of death duties, the Court said:

> "Of course, they concern the passing of property by death, for if there was no property to transmit, there would be nothing upon which the tax levied on the occasion of death could be computed."

In *Wardell v. Blum*, 276 Fed. 226, the Circuit Court of Appeals of the Ninth Circuit, in holding that a wife's share

in community property was not taxable as a part of her husband's estate under the Federal Law, said at page 227:

> "All inheritance taxes are imposed on the transfer of the net estate of the 'deceased', from which the conclusion is inevitable that the property upon which such a tax is imposed must, in truth, be the property of the deceased."

The law does not say anything about property passing at death. The tax is on the transfer into this trust. The only connection whatever between this tax and death is that death is used to describe the type of transfer which is taxed, and that death fixes the time for the payment of the tax.

Again in neither the Frick nor the Reed case can it be a tax upon the *"cessation of an interest"* at death. Mr. Frick had no interest in the policies which ceased at death. Mr. Reed had a life interest in the income of an irrevocable trust created in 1902. It was his life interest, and this alone, that ceased at death. What was that interest worth at the moment of death? What was its fair market value? Obviously nothing. May a million dollar tax be collected on the cessation of an interest worth nothing? But counsel may say his interest was in the whole trust and the whole trust was worth four million dollars. If the fact of having any interest draws into the estate the whole source of this interest we come to this absurdity:

Suppose Reed's interest, instead of being a right during his life to all the income, had been a right to one per cent of all the income for life. Could it then be contended that the value of the entire trust must be taxed when that meagre life estate ceased. Could it be reasonably contended that the same interest would have ceased in the supposed case of the right to one per cent of the income, as would have ceased if Reed had owned the four million dollars worth of assets unaffected by any trust? Obviously no. If the

interest which ceased on the day of his death, be valued as of that moment when *ex hypothesi* his expectancy was nothing, it must be found to be valueless. Then on what reasonable theory can it be taxed as though it were worth $4,000,000? We submit that on these facts the tax cannot be deemed to be a tax on the cessation of an interest.

After having considered the coming into possession theory, the uncompleted transfer theory, the measurement theory and the theories that the tax is on the passing of property at death or on the cessation of an interest, each of which does violence to the plain meaning of the words of the Act and fails to meet consistently the various calls of the statute, we submit that the law in reality compels the taxing of a past transfer—a past transaction. The group of cases considered by this Court with *Shwab v. Doyle, supra,* dealt with a variety of past transactions and in each instance held in substance that the *1916* law properly construed did *not* reach those transactions completed before its enactment; thus rejecting all these theories that a prospective occurrence was being taxed. When the 1918 Act is applied to a state of facts like those in the Reed case the statute necessarily raises the constitutional question. Congress in this instance has passed a statute expressly on the THEORY OF RETROACTIVE TAXATION. Is it constitutional?

II.

THE FEDERAL ESTATE TAX ACT IN TAXING GIFTS MADE BEFORE ITS ADOPTION IS UNCONSTITUTIONAL.

A.

IT IS AN UNAPPORTIONED DIRECT TAX.

We propose to give no long review of the various decisions of this Court dealing with the questions of direct as distinguished from indirect taxes. We believe that no complete and all-inclusive definition has ever been framed. We doubt if any ever can be framed until the scope of the legislator's ingenuity in devising tax laws can be defined and classified and the infinitude of combinations into which man's business transactions may fall, be accurately known.

We believe, however, that the greatest existing treatise on the subject is found in *Pollock v. Farmers Loan & Trust Co.*, 157 U. S. 429; 158 U. S. 601, and that all the learning that went before, may, after it went into that crucible, be passed over and the conclusions of that case be taken as at least the new starting place for discussion.

We submit that the mere difficulty of making scientific distinction between direct and indirect taxes is not controlling. In the very nature of the situation the definition must develop as new tax laws and new sets of fact come before this Court for consideration. A reading of the decisions of this Court shows that in a cloudy and obscure realm, a line of demarcation has gradually been worn. On the one side fall the cases of direct taxation, on the other those of indirect taxation. That a distinction exists and that the framers of the constitution intended the two different classes to be differently dealt with and to be subject to different limitations must be granted.

We believe that the following is the most complete definition of the distinction to be derived from the cases up to this time:

When a tax is absolute and inevitable, it is direct; when it is not absolute or inevitable, it is indirect. When the tax is imposed regardless of any act or failure to act on the taxpayer's part, it is direct; when it is imposed because the taxpayer's voluntary act or failure to act brings him within the terms of the law, it is indirect. In other words, when a man has the power so to arrange his transactions through the exercise of his own volition, as to bring them within or keep them without the taxable realm as covered by a given tax statute, that statute must be classified as one imposing an indirect tax. But when the creation or the bringing into being of the taxable status could not be avoided by the taxpayer, the tax is direct.

In the Pollock case, reported in 157 U. S., Chief Justice Fuller, at page 558, says:

> "Ordinarily all taxes paid primarily by persons who can shift the burden upon some one else, or who are *under no legal compulsion* to pay them, are considered indirect taxes; but a tax upon property holders in respect of their estates, whether real or personal, or of the income yielded by such estates, and *the payment of which cannot be avoided*, are direct taxes." (Italics ours.)

On the rehearing of the case, the Chief Justice, as reported in 158 U. S. at page 627, said:

> "Whatever the speculative views of political economists or revenue reformers may be, can it be properly held that the Constitution, taken in its plain and obvious sense, and with due regard to the circumstances attending the formation of the Government, authorizes a general unapportioned tax on the products of the farm and the rents of real estate,

although imposed merely because of ownership and with no possible means of escape from payment, as belonging to a totally different class from that which includes the property from whence the income proceeds?

"There can be but one answer, unless the constitutional restriction is to be treated as utterly illusory and futile, and the object of the framers defeated. We find it impossible to hold that a fundamental requisition, deemed so important as to be enforced by two provisions, one affirmative and one negative, can be refined away by forced distinctions between that which gives value to property, and the property itself." (Italics ours.)

In *South Carolina v. U. S.*, 39 Court of Claims, 257, it is said:

"A tax is obligatory; from it there is no escape. An excise is voluntary: the purchaser who would pay it cannot be compelled to purchase." (Affirmed in 199 U. S. 437.)

In *Thomas v. U. S.*, 192 U. S. 363, this Court has held valid a stamp duty on sales of corporate stock squarely on the ground that there was no absolute and unavoidable demand. Mr. Chief Justice Fuller said at page 371:

"The stamp duty is contingent on the happening of the event of sale, *and the element of absolute and unavoidable demand is lacking*. As such it falls, as stamp taxes ordinarily do, within the second class of the forms of taxation." (Italics ours.)

In *Flint v. Stone Tracy Co.*, 220 U. S. 107, this same test was applied in passing upon the validity of the Federal Excise tax on corporations. Mr. Justice Day said for the Court at page 151:

"The tax under consideration, as we have construed the statute, may be described as an excise upon the particular privilege of doing business in a corporate capacity, i. e., with the advantages which arise from corporate or quasi corporate organizations; or when applied to insurance companies, for doing the business of such companies. As was said in the Thomas case, 192 U. S. supra, the requirement to pay such taxes involves the exercise of privileges, and *the element of absolute and unavoidable demand is lacking.* If business is not done in the manner described in the statute, no tax is payable." (Italics ours.)

It may be helpful to give a moment's consideration to the *capitation* tax, expressly classified by the Constitution as a direct tax. What is it which makes a capitation tax a direct tax? Clearly it must be something in the nature of the tax, and not the mere fact that it is an isolated type of taxation included within direct taxation merely by an arbitrary classification. The essence of the capitation tax is the fact that it is a tax upon persons. Clearly the direct character of the tax is not changed by the fact that it may be limited to a certain class of persons, such as citizens of the United States or male citizens over twenty-one years of age. All will agree that such a tax is a direct tax. Suppose the class of persons taxed to be narrowed down to include only bachelors. Could any one doubt that this would be a direct tax? Or, suppose the tax were applied only to persons who had theretofore been married. This tax on a certain class of persons would be just as direct as any other capitation tax. In fact, a tax upon any class of persons classified according to their condition at the date of enactment of the tax law, or according to their past conditions or past actions, could be no different in principle. The same characteristic which makes the ordinary capitation tax a direct tax brings any unavoidable tax upon any determinable group of persons within the same category. This characteristic is the absolute and unavoidable demand.

When a past act is taxed, the taxpayer has no choice but to pay it. When the 1918 law was passed, Messrs. Frick and Reed and all other persons who had made similar contracts or transfers were made absolutely liable for the tax. Nothing they could have done or refrained from doing after they knew of this law would have altered their tax liability. The tax bore directly on the persons of Frick and Reed because no matter what happened or failed to happen after the passage of the law, the liability remained unaltered. When a law taxes all persons who have done certain acts in the past, the tax is not on the happening of any event, but is essentially a tax on a class of persons—persons classified by their past actions; and utterly unlike a tax on persons who *shall* import or *shall* manufacture or sell goods in the future. If this tax be indirect then a tax on all persons who obtained a divorce in the past or who had red hair in the past might be levied as an indirect tax. So considered the tax here is obviously more of a capitation than a privilege tax, for if there ever had been a privilege, it had long since been exercised and was non-existent when the Statute was passed. Furthermore, the privilege was never one granted by the Federal Government, the taxing sovereign. The fact that payment of the tax is postponed until death in no way alters the direct nature of the tax. The liability attached directly by the passage of the law and not indirectly by reason of some future event. The future event merely fixed the pay-day.

A tax on lands is a direct tax. A tax on the income from land is a direct tax; so is a tax on personal property or the income therefrom. A tax on property because of ownership is a property tax, a direct tax. Likewise, a tax on the exercise of an essential element of ownership is a property tax.

In *Dawson v. Kentucky Distilleries Co.*, 255 U. S. 288, a Kentucky statute taxing all liquor withdrawn from bond was involved. In holding the tax to be a property tax, Mr. Justice Brandeis for this Court said at page 294:

"In fact, the tax is one imposed upon each lot of whiskey at the time it is removed from bond within the state. The tax might be said to be upon the act of removal from the bonded warehouse within the State. But as stated by the lower Court, 'the thing really taxed is the act of the owner in taking his property out of storage into his own possession (absolute or qualified), for the purpose of making some one of the only uses of which it is capable; i. e., consumption, sale, or keeping for future consumption or sale * * *. The whole value of the whiskey depends upon the owner's right to get it from the place where the law has compelled him to put it, and to tax the right is to tax the value.' *To levy a tax by reason of ownership of property is to tax the property.*" (Italics ours.)

In *Craig v. Taylor & Sons*, 192 Ky. 36, the Supreme Court of Kentucky says (p. 39):

"The mere right to own and hold property cannot be made the subject of excises, since the levying of a tax by reason of ownership of property is to tax the property."

In *Thompson v. Kreutzer*, 112 Miss. 165, the Court says (p. 167):

"A tax on a thing is a tax on all its essential attributes; and a tax on an essential attribute of a thing is a tax on the thing itself. * * * No definition of property can be framed which does not include the right of ownership. Consequently, no tax can be imposed on the right of ownership which is not also a tax on property."

In *Eisner v. Macomber*, 252 U. S. 189, in holding that the tax on stock dividends was a direct tax not protected by the Sixteenth Amendment because stock dividends are not income, this Court answered the Government's agrument that the tax was indirect as follows (p. 217):

"* * * the Government, * * * virtually abandoning the contention that a stock dividend increases the interest of the stockholder or otherwise enriches him, insisted as an alternative that, by the true construction of the Act of 1916, the tax is imposed not upon the stock dividend, but rather upon the stockholder's share of the undivided profits previously accumulated by the corporation; the tax being levied as a matter of convenience at the time such profits became manifest through the stock dividend. If so construed, would the act be constitutional?

"That Congress has power to tax shareholders upon their property interests in the stock of corporations is beyond question; and that such interests might be valued in view of the condition of the company, including its accumulated and undivided profits, is equally clear. *But that this would be taxation of property because of ownership, and hence would require apportionment under the provisions of the Constitution is settled beyond peradventure by previous decisions of this Court.*" (Italics ours.)

In other words, a tax on past accumulations could not be a privilege tax, but was a direct tax.

Whatever may be said in favor of a tax upon a future optional disposal of one's property in a given way, it is a vastly different thing to tax the value of property disposed of *inter-vivos* in the past and simply because it was so disposed of. In the latter case, it is a tax on an essential attribute of property and therefore a tax on the property itself. If this be constitutional, why may not Congress place a tax on every one of us in respect of every house ever owned and lived in by any of us in the past?

We do not believe that under the guise of taxing a privilege, where the privilege either is non-existent because exercised before the law was passed, or was derived from

the State rather than from the Federal Government, Congress may evade the constitutional provisions. In the Child Labor Tax case in 259 U. S. 20, this Court refused to permit Congress under the guise of the taxing power to regulate the internal affairs of a state.

In the Pollock case, at 157 U. S. 581, this Court said:

> "If it be true that by varying the form the substance may be changed, it is not easy to see that anything would remain of the limitations of the Constitution, or of the rule of taxation and representation, so carefully recognized and guarded in favor of the citizens of each state. But constitutional provisions cannot be thus evaded. It is the substance and not the form which controls as has indeed been established by repeated decisions of this Court."

In *Dawson v. Kentucky Distilleries Co., supra,* at 255 U. S. 292, Mr. Justice Brandeis said:

> "The name by which the tax is described in the statute is, of course, immaterial. Its character must be determined by its incidents."

As said in *Kansas City Ry. Co. v. Botkin,* 240 U. S. 227, 235:

> "A tax may be in form a privilege tax and yet, in substance, may be a tax on property."

Unless we go counter to the principle that the substance and not the form is controlling, we may not brush aside the contention that the retroactive provisions of the 1918 Act impose a direct tax, by announcing that generically and historically death duties are and have always been regarded as indirect taxes and that therefore the tax under consideration is an indirect tax, and then cite *Knowlton v. Moore,* 178 U. S. 41 and *N. Y. Trust Company v. Eisner,* 256 U. S. 345, as authority.

The truth is, in our view, that the retroactive provisions of this law do not properly belong in a death duty statute at all. These provisions impose no death duties; they have nothing to do with death, except as death fixes a date for collection.

In the Knowlton case and in the Trust Co. v. Eisner case no question of retroactivity was present. *The language used in those cases had to do with prospective situations.*

The tax in neither of these cases was inevitable as in the present case. In each case the taxpayers' volition had a chance to operate. In the Eisner case, last above, this fact is brought out by the observation of Mr. Justice Holmes as to the testator. He says at 256 U. S. 349, "He (the testator) knows the law and the consequences of the disposition that he makes." These, we submit, constitute vital differences between those cases and the present case.

In the Frick case and in the Reed case we have absolutely inevitable taxes. The 1918 law was not in existence when the one took out his insurance policies, or the other created his trust. Both situations were beyond recall years before the law was passed. Neither decedent knew the 1918 law because when he consummated his contract there was no estate tax law to be known. Neither man knew or could know either the law or "the consequences of the disposition" that he made.

We are here suggesting no departure from the doctrine of *stare decisis*. We do not believe any decisions of this Court have ever held constitutional a law similar to the retroactive provisions of this law. But we submit that, regardless of how often other phases of this or any other similar statute may have been held to be constitutional, if a new state of facts be presented showing that the particular clause of the statute here under consideration may result in the infringement of a constitutional right of the latest litigant, the question must be examined in the light of the novel facts, and the constitutionality of the statute as applied to this situation determined.

Stockdale v. The Insurance Companies, 20 Wall. 323, turned on the use of the word "construed" in the statute. Was it "an invasion of the judicial function where the effect of the statute and the purpose of the statute are clearly within the legislative function", for the statute to say that certain sections shall be "construed" to impose certain taxes? The decision does not discuss direct or indirect taxes or argue the constitutional question. In any event, the decisions of this Court on income taxation, prior to the Pollock case, were overruled by the Pollock case.

The case of *Wright v. Blakeslee,* 101 U. S. 174, decided prior to the Pollock case, went off solely on a question of statutory construction and neither considered nor decided any constitutional point.

Such cases as *Brushaber v. Union Pacific Ry. Co.,* 240 U. S. 1, upholding the validity of income tax laws which are partially retroactive are not authority for retroactive *excise* taxes. Under the Sixteenth Amendment, Congress has power to levy income taxes, without apportionment, regardless of the fact of their being direct. We are not concerned here with the question of whether permissible *direct taxes* may also be retroactive.

In so far as the tax is collected from the beneficiary of life insurance or of a gift, it is clearly a direct tax. It has been expressly held that a tax on taking possession of one's own property is a direct tax; *Dawson v. Kentucky Distilleries Co.,* 255 U. S. 288, 294; *Craig v. Taylor & Sons,* 192 Ky. 36; *Thompson v. Kreutzer,* 112 Miss. 165; *Thompson v. McLeod,* 112 Miss. 283. *Matter of Pell,* 60 N. Y. App. Div. 286, affirmed 171 N. Y. 48, held that an inheritance tax on a beneficiary whose right was vested prior to the passage of the law was a direct tax. If a tax on the privilege of taking possession of property already owned is a direct tax, *a fortiori,* a tax on the estate of a decedent who exercises no privilege at all in connection with the property is a direct tax.

If this tax on past transfers is valid, Congress can in effect levy a direct tax without apportionment on any and all property in this country simply by putting it in the form of a retroactive excise tax. For example, Congress could tax all foreign made goods now in this country by calling it an excise on the past importation or on the past purchase of imported goods. Or Congress could levy a tax on all real estate by calling it an excise on the last recorded transfer of every parcel of real property. Such taxes would be the very things which the framers of the Constitution sought to prohibit by two distinct provisions. But the substance of constitutional restrictions cannot be nullified by indirect means. *The Child Labor Tax Case,* 259 U. S. 20; *Hill v. Wallace,* 259 U. S. 44. The direct tax provisions of the Constitution must be given some substantial meaning and effect. The test of absolute and unavoidable demand is the only test which conforms with history, with the adjudicated cases and with the purpose of these restrictions. Unless two express provisions of the Constitution are to be rendered meaningless and of no effect, there is no escape from the conclusion that the tax in the case at bar is an unconstitutional direct tax.

These constitutional restrictions must be given some real effect. As said in *Pollock v. Farmers Loan and Trust Company,* 157 U. S. 429, 583:

> "But the acceptance of the rule of apportionment was one of the compromises which made the adoption of the Constitution possible, and secured the creation of that dual form of government, so elastic and so strong, which has thus far survived in unabated vigor. If, by calling a tax indirect when it is essentially direct, the rule of protection could be frittered away, one of the great landmarks defining the boundary between the nation and the states of which it is composed, would have disappeared, and with it one of the bulwarks of private rights and private property."

In *Y. M. C. A. v. Davis,* 264 U. S. 47, this Court, in affirming the Supreme Court of Ohio which had decided that although the residuary estate went to charity, out of the residuary estate must come the Federal Estate tax assessed under the 1918 Act, speaks thus of the intent and purpose of Congress, at page 50:

> "It (Congress) was intending to favor gifts for altruistic objects, not by specific exemption of those gifts, but by encouraging testators to make such gifts. Congress was in reality *dealing with the testator before his death.* It said to him: 'If you *will make* such gifts, we'll reduce your death duties and measure them not by your whole estate, but by that amount, less what you give'." (Italics ours.)

The very use of this supposed colloquy between Congress and the taxpayer brings out with irresistible force the iniquity of the retroactive provisions of this law as applied to the case at bar. A possible paraphrase would be:

> "Mr. Reed, inasmuch as you *have already made* an irrevocable gift which at the time you made it was a legitimate gift and free from tax, we'll add to your death duties a tax not only on the value of what you gave away but on the later value of all the property into which your gift has grown and increased, whether the actual existing assets were ever yours or not and we'll do this knowing it is too late for you to retrace your steps and reclaim your gift, unless perchance the United States Constitution blocks our plan."

We submit that just as an income tax is a direct tax—a judicial conclusion upon which the states have now put the stamp of their approval through the ratification of the Sixteenth Amendment—so is a tax upon a past gift, or upon the proceeds of a previously created insurance contract, a direct tax and, unless apportioned, violative of the Constitution.

B.

THE RETROACTIVE PROVISIONS OF SECTION 402 OF THE 1918 FEDERAL ESTATE TAX LAW VIOLATE THE FIFTH AMENDMENT.

We shall contend in this portion of our brief that this tax upon a past, completed transfer of property amounts to an arbitrary exaction and operates to deprive the Frick estate and the Reed estate of property without due process of law. In making this contention, we know that the taxing power of Congress is broad. But even in the Brushaber case, *supra,* where a dictum was uttered as to the breadth of the taxing power, the Court added, at 240 U. S. 24:

> "This doctrine would have no application in a case where, although there was a seeming exercise of the taxing power, the act complained of was so arbitrary as to constrain to the conclusion that it was not the exertion of taxation, but a confiscation of property; that is a taking of the same in violation of the 5th Amendment; or what is equivalent thereto, was so wanting in basis for classification as to produce such a gross and patent inequality as to inevitably lead to the same conclusion."

On the other hand, we know of no actual decision of this Court holding that, outside of the prohibition of export taxes and the requirements of apportionment of direct taxes, and of uniformity of indirect taxes, Congress may act without restriction in taxation matters. A Federal tax law which afforded the taxpayer no opportunity to be heard, would certainly be held to be bad as a taking without due process. Furthermore, to suggest that the grant of the power to tax be read with the Fifth Amendment and that the two be construed together is not only in keeping with the well established principles of constitutional construction, but accords with the well established precedent as to the construction of the war power of Congress.

In *Proutt v. Starr,* 188 U. S. 537, 543, 544, it was said:

> "The Constitution of the United States, with the several amendments thereof must be regarded as one instrument, all of whose provisions are to be deemed of equal validity * * * (and that) it is one of the important functions of this Court to so interpret the various provisions and limitations contained in the organic law of the union that each and all shall be respected and observed."

The Constitution's broad grant of the war power, just as essential a power as the taxing power though not as often used, has been deemed limited by the Fifth Amendment.

> *Ex Parte Milligan,* 4 Wall 2, 121-127.
> *United States v. Russell,* 13 Wall. 623, 627.
> *Hamilton v. Kentucky Distilleries Co.,* 251 U. S. 146, 155, 156.

In *United States v. Cohen Grocery Co.,* 255 U. S. 81, 88, Mr. Chief Justice White said:

> "We are of opinion that the Court below was clearly right in ruling that the decisions of this Court indisputably establish that the mere existence of a state of war could not suspend or change the operation upon the power of Congress of the guarantees and limitations of the 5th and 6th Amendments as to questions such as we are here passing upon."

The phrase "Due process of law", whether used in the Fifth or the Fourteenth Amendment means the same thing. Referring to this phrase in *Hurtado v. People of California,* 110 U. S. 516, the Court said at page 534:

> "The conclusion is equally irresistible, that when the same phrase was employed in the 14th Amendment to restrain the action of the states, it was used in the same sense and with no greater extent. * * *"

As said by Judge Anderson in *U. S. v. Armstrong,* 265 Fed. 683, 690:

"By the simplest and plainest rules of construction, the words 'due process of law' must have the same meaning in the Fifth and the Fourteenth Amendments."

To the same effect are *Carrol v. Greenwich Ins. Co.*, 199 U. S. 401, 410, and *Ex Parte Kemmler*, 136 U. S. 436.

The vast weight of authority holds that retroactive inheritance tax laws of the *states*, similar to the Federal Act now under discussion, are unconstitutional under the provisions of the Fourteenth Amendment, as a taking of property without due process of law or a taking of private property for public use without just compensation.

The most celebrated of the cases is *Matter of Pell*, 171 N. Y. 48.

In re *Craig's Estate*, 97 N. Y. App. Div. 289 (Affd. 181 N. Y. 551), involved a trust almost identical with the Reed trust. After the trust was created and before decedent's death, New York passed a statute imposing an inheritance tax. In holding the tax invalid, the Court said at page 291:

"In the discussion the appellants must be regarded on May 9, 1885, as being in the same position as they would have been in if the remainders had been acquired by purchase instead of gift, and it cannot be that the state can levy an assessment upon the right of a citizen to enjoy the fruits of a prior purchase, which, when made, was wholly free from such an imposition."

Again at page 296 the Appellate Division of the Court said:

"The underlying principle which supports the tax is that such right is not a natural one but is in fact a privilege only, and that the authority conferring the privilege may impose conditions upon its

exercise. But when the privilege has ripened into a right it is too late to impose conditions of the character in question, and when the right is conferred by a lawfully executed grant or contract it is property, and not a privilege, and as such is protected from legislative encroachment by constitutional guaranties."

The Supreme Court of California held unconstitutional a similar statute in *Hunt v. Wicht*, 174 Calif. 205. At 209 the Court said:

> "The right of the grantee to have actual physical possession of the property itself, and enjoyment of the other incidents of an estate for life upon the death of the life tenant was absolutely vested by the delivery of the deed in escrow, and nondefeasible, and the Legislature could not thereafter lawfully destroy, impair or burden this property right under the guise of a succession tax on account of the transfer."

In *Lacey v. State Treasurer*, 152 Iowa 477, the Supreme Court of Iowa in holding a similar law unconstitutional said at page 483:

> "If the right to the property passed by the conveyance beyond the control of the grantor, it was a vested right; it was not a mere expectancy, like the prospective right of an heir, or the inchoate right of a wife, and it was therefore not subject to burdens which the Legislature might attempt to impose by retrospective laws."

In accord are:

Miller v. McLaughlin, 141 Mich. 425.
Commonwealth v. Wellford, 114 Va. 372.
State v. Safe Deposit & Trust Co., 132 Md. 251.
Commonwealth v. McCauley's Executors, 166 Ky. 450.
Eury's Executors v. State, 72 Ohio State 448.

State v. Probate Court, 102 Minn. 268, was a similar holding. The Court said (p. 285):

> "That law is prospective in its operation, and it is beyond the power of the state, even if it so desired, to subject to its operation property which the owner in good faith disposed of before his death."

In re Lansing's Estate, 182 N. Y. 238, is a similar holding. The Court said:

> "The law sanctioned the gift of Mr. Suffern when it was made, and the law cannot cut down the gift by imposing a transfer tax when there was no transfer."

People v. Trust Company of America, 205 N. Y. 74. The New York law imposed a tax on future advances made under existing mortgages. The state sought by this suit to collect a tax from the mortgagee on additional bonds issued under the terms of a mortgage executed before the law was passed. In holding the tax invalid, the Court said (p. 77):

> "The legislature could not impose a tax upon the defendant for a transaction which at the time it was effected was subject to no tax."

In *Blair v. Harold,* 150 Fed. 199, the decedent made a partnership agreement with his son and others under which, on decedent's death, his share was to go to his son. After the making of this agreement and shortly before decedent's death, Congress passed the Act of 1898 imposing an inheritance tax on transfers to take effect at death.

The lower court held illegal the tax on the share derived by the son and cited the Pell case with approval. The Court of Appeals for the 3rd Circuit in affirming the case, 158 Fed. 804, said at page 806:

"It cannot be supposed that this partnership agreement was designed to circumvent a statute enacted several years after it was made. It was entered into in good faith, and the rights of the plaintiff then accrued. As was said by the learned District Judge, 'they were absolute and irrevocable so far as the parties were concerned, and were contingent only upon the happening of an event which did happen.' They were acquired by contract, and not by last will and testament, or otherwise." (Italics ours.)

The cases decided by the State Courts and holding similar retroactive statutes illegal as an interference with vested rights must all be erroneous if the retroactive law now under consideration be valid.

In *Billings v. U. S.*, 232 U. S. 261, sometimes referred to as authorizing a retroactive excise tax, the statute specified a future date for the payment of a tax. It fell on any one using a foreign built yacht. The yacht was used after the enactment of the Statute. Hence only its prospective operation was involved in that case.

We deem it unnecessary at length to discuss those cases of so-called limited retroactivity where this Court has sustained tax laws passed during a current fiscal period, and made to apply from the beginning of the period. The Brushaber case, *supra,* illustrates these cases. There the taxable process was continuing and not yet terminated. In the very nature of the case, those instances naturally fall in a distinct class and we submit afford no precedent for sustaining the 1918 law, as it affects a past, completed act. Furthermore, as previously suggested, where they have to do with income taxes they involve permissible direct taxes. One of the great vices incident to this law as a retroactive so-called excise law is that it is a tax on something that is non-existent, viz., a previously exercised privilege.

C.

THE RETROACTIVE PROVISIONS OF THE 1918 ESTATE TAX LAW VIOLATE THE FUNDAMENTAL CONCEPTIONS OF FREE GOVERNMENT.

There has grown up in the decisions of this and other courts, a group of pronouncements to the effect that there are certain things which the legislative body may not do, simply because they are too arbitrary, too unreasonable, too unthinkable to be sanctioned by the fundamental and guiding principles of civilized society. We believe that these pronouncements may properly be classified as a body of principles formulated under that wisely elastic phrase "due process of law"; but for purposes of emphasis we shall discuss them under the foregoing heading.

In *Shwab v. Doyle, supra,* this Court has expressed itself in no uncertain terms regarding retrospective laws, when it quoted with approval the following language of Justice Story (258 U. S. 534):

> "Retrospective laws are, indeed, generally unjust; and, as has been forcibly said, neither accord with sound legislation nor with the fundamental principles of the social compact."

This was said in answer to the Government's contention that the 1916 Estate Tax law be given a retroactive effect.

Cooley, at page 41 of his work on Taxation, said:

> "Vast as is the power of the Government to levy taxes upon its citizens, there are nevertheless limitations upon it of a very distinct and positive character, which inhere in the very nature of the power itself. Some of these limitations are commonly declared in the written constitution, but the declaration is rather from abundant caution than from necessity, as the limitations are equally imperative whether thus declared or not."

This was illustrated in the Child Labor Tax case, *supra.*

In the *Pollock* case, *supra,* Mr. Justice Field said at 157 U. S. 599:

> "As stated by counsel: 'There is no such thing in the theory of our national government as unlimited power of taxation in Congress. There are limitations, as he justly observes, of its powers arising out of the essential nature of all free governments; there are reservations of individual rights, without which society could not exist, and which are respected by every government. The right of taxation is subject to these limitations.' *Citizens Sav. L. Assn. of Cleveland v. Topeka,* 87 U. S. 20 Wall. 655 (22:455) and *Parkersburg v. Brown,* 106 U. S. 487 (37:238)."

In *Knowlton v. Moore,* Chief Justice White pointed out the arbitrary character of a law which would base a tax not only on what a legatee received but upon the whole estate of the decedent. In conclusion, he said at 178 U. S. 77:

> "It may be doubted by some, aside from express constitutional restrictions, whether the taxation by Congress of the property of one person, accompanied with an arbitrary provision that the rate of tax shall be fixed with reference to the sum of the property of another, thus bringing about the profound inequality which we have noticed, would not transcend the limitations arising from those fundamental conceptions of free government which underlie all constitutional systems."

In the Frick case a part of the tax levied in respect to life insurance must come out of the beneficiaries of those policies under the reimbursement clause of Section 408. In the Reed case, if the residuary estate had been insufficient the tax would have had to be paid by the trustee out of the trust fund under the provisions of Section 409.

In other words, we have the very question raised as to these transferees or beneficiaries that was present in the Knowlton case. The Government in effect insists that the rate of the tax should be based not upon the property received by the beneficiary, but upon the value of the whole estate.

Chief Justice White pointed out the vice of this in that oft quoted passage from the *Knowlton* case on page 76 as follows:

> "The tax is on each separate legacy or distributive share, but the rate is measured by the whole estate. In other words, the construction proceeds upon the assumption that Congress intended to tax the separate legacies, not by their own value, but by that of a wholly distinct and separate thing. But this is equivalent to saying that the principle underlying the asserted interpretation is that the house of A, which is only worth \$1,000, may be taxed, but that the rate of the tax is to be determined by attributing to A's house the value of B's house, which may be worth a hundred fold the amount. The gross inequalities which must inevitably result from the admission of this theory are readily illustrated. Thus a person dying and leaving an estate of \$10,500, bequeaths to a hospital \$10,000. The rate of tax would be five per cent, and the amount of tax \$500. Another person dies at the same time, leaves an estate of \$1,000,000 and bequeaths \$10,000 to the same institution. The rate of tax would be 12½ per cent, and the amount of the tax \$1,250. It would thus come to pass that the same person, occupying the same relation, and taking in the same character two equal sums from two different persons, would pay in the one case more than twice the tax that he would in the other."

This is exactly the sort of thing that is illustrated by the Frick estate; the size of the residuary estate in which

the insurance beneficiaries might have no interest determines the tax which the insurance beneficiaries must pay.

In the earlier case of *Hartman v. Greenhow,* 102 U. S. 672, Mr. Justice Field said at page 684:

> "And surely it is not necessary to argue that an act which requires the holder of one contract to pay the taxes levied upon another contract held by a stranger cannot be sustained. *Such an Act is not a legitimate exercise of the taxing power;* it undertakes to impose upon one the burden which should fall, if at all, upon another."

In *U. S. v. Baltimore & Ohio Railroad Company,* 17 Wall 322, Mr. Justice Hunt said at page 326:

> "It is not taxation that government should take from one the profits and gains of another."

In the Reed case if this tax were collected from the trustee or its beneficiaries, it is taxing A on a past act of B. Collecting the tax from the estate as has been done, is taxing B on property owned by A. The executrix has paid a tax, the rate of which might, and the amount of which did, depend on the value of the assets in the trust, in which the executrix as such has never had any interest and over which she has had no control. Not only this; the amount of the tax was figured on the incremented value of the assets in the trust at the date of the decedent's death, and that value was approximately double the value that he had ever owned.

If Congress attempted to levy a tax on the transactions of red-headed men, we believe this Court would find a constitutional limitation upon the exercise of such power. Is not Congress, in substance, attempting to do this very thing here in taxing all persons who happen to have done certain things before the law was psased?

In the case of *Coolidge v. Nichols,* referred to above, decided Jan. 28, 1925, by the Federal District Court of Massa-

chusetts, and not yet reported, the gift in trust reserving a life interest to the donor was made in 1907. In 1917 all remaining interest of the donor in the trust was assigned to the original remaindermen. The assets originally placed in the trust were valued as of the date of the donor's death, which took place after the passage of the 1918 law, and being treated as part of the gross estate an additional tax was levied and collected in respect thereto. In charging the jury in a suit by the executor to recover this additional tax Judge Brewster said:

> "In every case of transmission by will, intestate laws or transfers to take effect after death or in contemplation of death, a power right or privilege has been exerted or exercised. *When one has availed himself of this privilege with knowledge of the tax, actual or constructive, he has voluntarily subjected himself to its burden,* and a statute which includes in the measure of the tax the value of the property thus transferred may well be deemed to have provided a reasonable classification, and this even if the decedent has entirely parted with all interest in the property; *but when one has, prior to the imposition of the tax, parted with all control over or interest in the property, the classification becomes arbitrary and unreasonable. Such arbitrary inclusion of property of others has been held in other jurisdictions invalid as unconstitutional.* * * *
>
> "As a result, I have reached the conclusion that the retroactive provisions of the act of 1918, so far as they apply to a transaction entirely completed before the passage of the Act, are unconstitutional and void. * * *" (Italics ours.)

It is immaterial whether such an exaction be termed a confiscation rather than a tax, or be held to violate the Fifth Amendment, or be held a violation of "Those fundamental conceptions of free government which underlie all

constitutional systems." (*Knowlton v. Moore,* 178 U. S. 41, 77.) In any event, it is an unreasonable and unwarranted exercise of legislative power and not the legitimate use of the taxing power.

CONCLUSION.

The retroactive provisions of the 1918 Federal Estate Tax Act when applied to situations such as those presented by the Frick case or by the Reed case, impose taxes upon transfers and gifts completed before the enactment of the law. The tax is absolute and unavoidable. It leaves open to the taxpayer no option of creating or of foregoing the creating of a taxable situation. It taxes him merely because of the past exercise of one of the attributes of the ownership of property. It therefore falls in the category of direct taxes and being unapportioned is unconstitutional.

These retroactive provisions impose consequences upon the legitimate, prior acts of men utterly beyond their possible contemplation. As a result, property is taken under the guise of taxation and taken in a way which violates the fundamental conceptions of organized society. We contend that this is a taking in violation of the 5th Amendment of the Constitution.

For some good reason the Almighty dropped a curtain before our eyes and concealed the future from us. The whole scheme of human life is worked out on this basis. This has its advantages and its apparent disadvantages, but regardless of the theoretical preponderance one way or the other, the fact is we cannot successfully peer into the future. Political institutions and man-made laws of necessity must be worked out in the light of the foregoing fact. A disregard of it is so inherently opposed to reason as to be almost inconceivable. Men have to live and plan their daily lives in the light of what they know or may fairly be presumed to know. They have to arrange their affairs, make their decisions, choose between one course of conduct

and another in the light of present conditions, modified to some extent possibly by the cloudy half light of a guess as to the future.

A man in 1902 makes a contract in the form of a trust or of an insurance policy. He complies with the law. He parts with his property under certain specified conditions; he does it irrevocably. He acts in the light of conditions present to him in 1902; the laws then existing are read into his trust or into his insurance policy. No estate tax law exists then or until fourteen years later. He does not know about it because it is unknowable. He makes his calculations and arranges his affairs in necessary ignorance of what is to be. He does not evade. There is nothing to attempt to evade. Then in 1916, or 1918, a Congress comes into being and by the enactment of a law gives a quality to the acts of these men never intended or guessed at by them and fastens upon those acts serious consequences which were never in their contemplation.

Was it not the recognition of such possibilities in analogous stiuations, that put into the Constitution the inhibition against the impairment of the obligation of contracts and the inhibition against Ex post facto laws? Do not the provisions of the Statute under consideration "transcend the limitations arising from those fundamental conceptions of free government which underlie all constitutional systems"?

We submit that the judgment of the Court below should be affirmed, if not on the authority of *Knox v. McElligott*, 258 U. S. 546, to the effect that Section 402 (f) rightly construed is not retroactive, then on the ground that the Section applied retroactively is unconstitutional.

Respectfully submitted,

Tyson S. Dines,
Peter H. Holme,
Harold D. Roberts,
Charles E. Works,
Amici Curiae.

Supreme Court of the United States,

OCTOBER TERM 1924—No. 681.

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C. G. LEWELLYN, FORMERLY COLLECTOR, ETC.,
Plaintiff in Error,

vs.

ADELAIDE H. C. FRICK, *et al.*, EXECUTORS,
Defendants in Error.

In Error to the District Court of the United States for the Western District of Pennsylvania.

BRIEF IN SUPPORT OF THE PROPOSITION

That the "Estate Tax" imposed by the Revenue Act of 1918 on the proceeds of life insurance payable directly to beneficiaries (other than to the decedent's estate), is void because (1) it is a "direct" tax levied solely because of the ownership of property and (2) it is measured by the value of the decedent's estate and not by any standard having reference to the beneficiaries who must pay it.

WM. MARSHALL BULLITT,
Amicus curiæ,
In behalf of the Association of Life Insurance Presidents.

The Evening Post Job Printing Office, Inc., 154 Fulton St., New York, N. Y.

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LIST OF AUTHORITIES.

Supreme Court of the United States.

OCTOBER TERM 1924: No. 681

C. G. LEWELLYN, formerly Collector, etc.,
Plaintiff in error,

against

ADELAIDE H. C. FRICK, *et al.*, Executors,
Defendants in error.

In error to the District Court of the United States for the Western District of Pennsylvania.

BRIEF FOR ASSOCIATION OF LIFE INSURANCE PRESIDENTS.

This case involves the question whether so much of §§ 402 (*f*), 408, 409 of the Estate Tax provisions of the Revenue Act of 1918 (40 Stat. 1096) as imposes a 25% tax upon $434,629.52 life insurance policies owned exclusively by *living* beneficiaries, under contracts with the insurance companies, and *forming no part of the decedent's estate,* is a "direct" tax or an excise tax.

STATEMENT OF THE CASE.

1. *The 25% Inheritance Tax ($108,657.38) upon the $434,629.52 life insurance payable to Mr. Frick's wife and daughter.* On December 2, 1919, H. C. Frick died leaving $97,000,000, with a net taxable estate of $28,629,594.73, so that the inheritance tax, on the excess over $10,000,000, was 25% (R. 23; § 401, 40 Stat. 1097).

The executors were compelled by § 402 (*f*) to include, as assets of the Frick estate, $434,629.52 (out of $474,629.52) life insurance that was payable to and owned by Mrs. Frick and Miss Frick; and to pay $108,657.38 as the 25% tax thereon, even though such insurance was *no part* of the Frick estate and never came into the executors' hands, but was paid directly by the insurance companies to the beneficiaries named in the policies, to-wit, the wife and daughter (R. 22-23).

In short, the law compelled the executors to increase the Frick Estate by the fictitious addition thereto of $434,629.52*, which never was any part of the Frick

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* *The Insurance Policies Involved.* At various dates between 1874-1901, and long before the passage of the Act, eight mutual life insurance companies issued eleven policies (aggregating with deferred dividends thereon, $474,629.52) on the life of H. C. Frick, which policies may be briefly summarized in four classes as follows (R. 15-21):

No. Policies.	Date.	Original Beneficiary.	Beneficiary (at date of Act and at death).	Powers, if any, reserved to Mr. Frick over policy or its proceeds.	
1	1901	Wife	Wife	None; no premium ever paid by Mr. Frick (R. 19)......	$114,000.00
1	1885	Wife	Wife	None; except usual options *re* cash values at end of tontine period in 1900, which were never exercised (R. 19)......	78,044.01

assets and to pay $108,657.38 taxes on such fictitious addition.

The executors paid the tax under protest and brought suit to recover it back (R. 2-12). The case was heard upon an agreed statement of facts (R. 14-24, 28).

No. Policies.	Date.	Original Beneficiary.	Beneficiary (at date of Act and at death).	Powers, if any, reserved to Mr. Frick over policy or its proceeds.	
1	1874	Estate	Wife	None; *assigned* policy to wife in 1882 (R. 16)	15,202.28
1	1874	Estate	Wife	None; except usual options *re* cash values at end of tontine period in 1894, which were never exercised. *Assigned* policy to wife in 1882 (R. 20)...........	13,581.80
4	1890-2	Estate	Daughter	Usual options *re* cash values at end of tontine periods, which were never exercised. *Assigned* policy to daughter on June 19, 1917, reserving right to revoke assignment but never did so (R. 17, 18, 20, 22)............	$189,825.16
3	1890-5	Estate	Daughter	None; except usual options *re* cash values at end of tontine periods which were never exercised. Daughter *designated* as beneficiary on June 19, 1917, and *no* right reserved to change beneficiary (R. 15, 17, 18).....	63,976.27
11	1874-1901	Total insurance payable to wife and daughter.			$474,629.52

They thus consist of four classes of policies, all completely vested before the passage of the Act, to-wit policies (1) originally taken out in the name of a beneficiary *other* than Mr. Frick's estate, with no power in him to change the beneficiary; (2) originally payable to Mr. Frick's estate and assigned by him to his wife, with no power reserved to change the beneficiary or revoke the assignment; (3) similar to (2) but reserving the power to revoke the assignment; and (4) originally payable to Mr. Frick's estate, but by supplemental contract with the company, made payable to his daughter as beneficiary with no power reserved to revoke or change such beneficiary.

The District Court (THOMPSON, *J.*) held that as the insurance was no part of the Frick estate, but was vested in, and belonged to, the wife and daughter long before his death, therefore, the tax thereon was not an excise or death duty, but was a *direct property tax* on the insurance proceeds; and consequently void because not apportioned as required by the Constitution, Article 1, §§ 2, 9 (R. 29-36).

2. *The Meaning of the Act.* There is no dispute as to the meaning of the Act. It includes in the net estate, and hence taxes, [at the highest bracket applicable to the estate], all the insurance (in excess of $40,000) payable to beneficiaries, on policies taken out by the insured on his life (§ 402 (*f*)).

It requires the executor to pay the tax (§ 407); in which event, he can recover from the beneficiaries such portion of the tax paid as the proceeds (in excess of $40,000) bear to the total estate (§ 408), which does not mean the entire tax but only a part thereof (p. note, *infra*). If the tax is not paid by the executor, the beneficiaries are personally liable and the policies are subject to a lien therefor (§ 409).

3. *The Questions presented.* Two questions arise. *First*: Is it a "direct" tax or an "excise"? *Second*: *If* an excise, is the measure of the tax valid?

The "Estate Tax" Provisions of Revenue Act of 1918.

(40 Stat. 1096)

"Sec. 401. That (in lieu of the tax imposed by Title II of the Revenue Act of 1916, as amended, and in lieu of the tax imposed by Title IX of the Revenue Act of 1917) *a tax* equal to the sum of the following percentages of the values of the net estate (determined as provided in section 403) *is hereby imposed upon the transfer* of the *net* estate of every decedent dying after the passage of this Act, whether a resident or nonresident of the United States:

1 per centum of the amount of the net estate not in excess of $50,000

(*Here follow the graduated rates and amounts from $50,000 up to $10,000,000*)

25 per centum of the amount by which the net estate exceeds $10,000,000. * * *

Sec. 402. That the *value* of the *gross* estate of the decedent shall be determined by *including* the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated. * * *

(*f*) To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess, over $40,000, of the amount *receivable by all other beneficiaries* as insurance under policies taken out by the decedent upon his own life.

Sec. 403. That for the purpose of the tax the value of the *net* estate shall be determined * * *

[by *deducting* from the *gross* estate determined as provided in Sec. 402, certain amounts for debts, expenses, losses, charitable gifts, etc., and a specific exemption of $50,000.]

Sec. 407. That the executor shall pay the tax to the collector or deputy collector * * *

Sec. 408 * * * If any part of the gross estate consists of proceeds of policies of insurance upon the life of the decedent receivable by a beneficiary other than the executor, the executor shall be entitled to recover from such beneficiary such portion of the total tax paid as the proceeds, in excess of $40,000, of such policies bear to the net estate. If there is more than one such beneficiary the executor shall be entitled to recover from such beneficiaries in the same ratio.

Sec. 409. * * * (*b*) if insurance passes under a contract executed by the decedent in favor of a specific beneficiary, and if in either case the tax in respect thereto is not paid when due, then the transferee, trustee, or beneficiary shall be personally liable for such tax, and such property, to the extent of the decedent's interest therein at the time of such transfer or to the extent of such beneficiary's interest under such contract of insurance, shall be subject to a like lien equal to the amount of such tax."

The method then is:

(1) Ascertain the *gross* estate by *including* certain elements therein defined, especially life insurance payable to third persons; [§ 402]; next,

(2) Ascertain the *net* estate, by *deducting* certain exemptions therein specified, from the *gross* estate as already determined in (1) [§ 403];

(3) Ascertain the tax by applying to such *net* estate determined in (2), the progressive rates set forth in § 401:

(4) Executor will pay the tax found in (3) [§ 407]:

(5) Executor may recover from the beneficiaries a certain part of the tax paid under (4) [§ 408]:

(6) If the executor fails to pay the tax, then the beneficiary is personally liable for that part of it in respect of the insurance, and a lien in favor of the United States arises upon such insurance or its proceeds [§ 409].

4. *Ultimately the tax burden is divided between the estate and beneficiaries.* § 408 gave to the executors the right to recover from the beneficiaries named in the policies, not the full $108,657.38 inheritance tax which the executors were compelled to pay with respect of the $434,629.52 insurance that never was any part of the estate, but only "such portion of the total tax paid as the proceeds, in excess of $40,000 of such policies bear to the net estate," to-wit, $96,230.80*. This would make the estate bear $12,426.58 or 11.44%, although it did not get a dollar of the insurance; and the wife and daughter bear $96,230.80 or 88.56%, even if they did not receive a dollar of the estate—all because Mr. Frick happened to be a very rich man.

In this particular case, owing to the specific provision in Mr. Frick's will (approved in *Y. M. C. A. v. Davis,* 264 U. S. 47, 51) that (R. 24)

> "All inheritance, legacy, succession or other duties or taxes * * * shall be paid out of the capital of my residuary estate,"

---

* This is arrived at as follows:

Recovery.		Total tax.		Proceeds.		Net estate.
X	:	$6,338,898.68	::	$434,629.52	:	$28,629,594.73

Solving the problem arithmetically shows that the proceeds (in excess of $40,000) of the policies is 1.5181% of the net estate; hence the amount recoverable by the executors from the beneficiaries is 1.5181% of the $6,338,898.68 tax paid, or $96,230.80 instead of the $108,657.38; leaving $12,426.58 to be borne by the executors.

the executors did not recover from the wife and daughter any part of the $108,657.38 which was paid out of the residuary estate; and, if now recovered by this suit it will go to the residuary legatees, Princeton University and various charities.

5. *The Government's contention.* The Government contends (1) that the tax is not a direct tax but is an excise tax (within *Knowlton* v. *Moore,* 178 U. S. 41; *Greiner* v. *Lewellyn,* 258 U. S. 384, and cases therein cited) measured by the value of the decedent's net estate (2) that it is lawful to include in such measure, *i. e.,* net estate, something that is not a part of the estate and is not itself taxable, on the theory that a tax may be measured by any standard Congress chooses to adopt even though it embraces something that is not itself taxable; (3) that the method of collecting the tax either from the executor (who receives none of the insurance) or from the beneficiaries (who *may* receive none of the estate) has no effect on the validity of its imposition.

SUMMARY OF POINTS DISCUSSED.

1. The 25% tax imposed by §§ 402 (f), 408, 409 on life insurance policies (payable to beneficiaries other than the decedent) is a direct tax on property by virtue of its ownership, and is void because not apportioned (pp. 10-23, infra).

2. The 25% tax imposed on beneficiaries' life insurance is neither a death duty nor a succession tax as those terms are defined in Scholey v. Rew, Knowlton v. Moore, New York Trust Co. v. Eisner or in any other decision of this court; and hence this tax cannot be sustained as an "Excise" tax on the authority of those cases (pp. 24-49, infra).

3. The 25% tax on the life insurance owned by the beneficiaries is void because of the basis on which it is calculated (pp. 50-54, infra).

FIRST POINT.

The 25% tax imposed by §§ 402 (f), 408, 409 on life insurance policies (payable to beneficiaries other than the decedent) is a direct tax on property by virtue of its ownership, and is void because not apportioned.

The Act imposes an *ad valorem* progressive graduated tax of from 1% to 25% on the proceeds of all* life insurance policies receivable by *living* beneficiaries, *i. e.*, family, creditors, partners, corporations, etc. having an insurable interest in a decedent's life.

The $108,657.38 tax is levied on the wife and daughters' insurance money ($434,629.52) merely because those women owned the policies; and from the standpoint of common sense, the tax is just as direct as if a 25% tax had been levied on a similar amount which they might have received from maturing corporate bonds or from an insurance company on account of

* For brevity, there will be omitted throughout any reference (1) to the $40,000 statutory exemption as irrelevant to the constitutional question; and (2) to policies payable to an insured or his executor as they are concededly taxable as a part of the decedent's estate.

matured endowment policies taken out by them on their own lives.*

Is that, in a constitutional sense, (1) a "direct" tax or (2) an "excise" tax?†

It is useless to indulge in abstract theoretical or economic speculations as to what are "direct" or "indirect" taxes. Resort must be had to history, to the prior decisions of this court, and to ordinary common sense, in order to determine whether the kind of tax here involved falls on this side, or that side, of the line which

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*Payments by life insurance companies to beneficiaries cannot be deemed "income" in any constitutional sense (*Eisner* v. *Macomber*, 252 U. S. 189, 206; *Towne* v. *Eisner*, 245 U. S. 418, 425; *Doyle* v. *Mitchell Bros. Co.*, 247 U. S. 179, 185; *Southern Pac. Co.* v. *Lowe*, 247 U. S. 330, 335; *U. S.* v. *Phellis*, 257 U. S. 156, 168; *Merchants' L. & T. Co.* v. *Smietanka*, 255 U. S. 509; *U. S.* v. *Supplee-Biddle Co.*, 265 U. S. 189, 194-5), but even if deemed income [and hence taxable without apportionment, 16th Amendment; *Brushaber* v. *Union Pacific*, 240 U. S. 1, 18; *Stanton* v. *Baltic Mining Co.*, 240 U. S. 103, 112, 113], then life insurance proceeds are expressly *exempted* by statute from taxation as income, because the "Income Tax" provisions of the Revenue Act of 1918 expressly provide that the very comprehensive language defining gross income (40 Stat. 1065),

"*Does not include* the following items, which shall be *exempt from taxation* under this title:

(1) The *proceeds of life insurance policies* paid upon the death of the insured to *individual beneficiaries* or to the estate of the insured;

(2) The amount received by the insured as a return of premium or premiums paid by him under life insurance, endowment, or annuity contracts, either during the term or at the maturity of the term mentioned in the contract or upon surrender of the contract."

U. S. v. *Supplee-Biddle Co.*, 265 U. S. 189, 195, is absolutely conclusive on this point.

†It is clearly not a "duty" or "impost", as those are synonymous terms and are both definable as taxes levied on articles imported from foreign countries.

was drawn by the framers of the Constitution between the two great classes of taxation, whose imposition was limited by apportionment and geographical uniformity respectively; because, as this Court has aptly said,

> "Upon this point a page of history is worth a volume of logic" (*New York Trust Co.* v. *Eisner,* 256 U. S. 349)
>
> "Taxation is eminently practical, and is in fact brought to every man's door, and for the purpose of deciding upon its validity a tax should be regarded in its *actual, practical* results, rather than with reference to those theoretical or abstract ideas whose correctness is the subject of dispute and contradiction among those who are experts in the science of political economy." (*Nicol* v. *Ames,* 173 U. S. 509, 516).

To emphasize that direct taxes must not be imposed except by apportionment, and that such a limitation meant something very real in the taxing life of the nation, the Constitution, not once, but *twice* (the only instance of duplication of provision in that instrument), declared that one of the two great divisions of the taxing power should never be exercised save by apportionment (Art. I):

> "Representatives and direct taxes *shall be apportioned* among the Several States * * * (§2)
>
> "No capitation, or other *direct* Tax shall be laid *unless* in proportion to the Census, * * *" (§9)

That limitation is a living thing and should not be frittered away by metaphysical subtleties seeking, in each

successive instance, to establish as "indirect" taxation, that which in its actual, practical results as brought home to every man's door in an eminently practical sense, is a "direct" tax on him, by taking away a part of his accumulated wealth simply because he owns it (*Pollock* v. *Farmers Loan & Trust Co.*, 158 U. S. 601, 628; *Nicol* v. *Ames*, 173 U. S. 509, 516; *Eisner* v. *Macomber*, 252 U. S. 189, 206).

The only express prohibitions laid by the Constitution on the grant of the taxing power to Congress were (1) that no direct tax should be laid except by apportionment and (2) that no tax should be laid on exports. This Court has enforced both prohibitions. Certainly if a stamp tax on foreign bills of lading, on policies of marine insurance, and on charter parties is *not* an *indirect* tax, as in form it is, but is a *direct* tax on the articles described in the bills of lading or insurance policies, or carried by the ships, then a 25% tax on the proceeds of policies is a direct tax.

Since the *Pollock* cases (157 U. S. 429; 158 U. S. 601), as interpreted in the cases cited in the margin,* it is settled that a percentage tax on personal property, merely because of its ownership, is a *direct* tax and must be apportioned.

The name by which the tax is described in the statute is, of course, immaterial. Its character must be determined by its incidents (*Dawson* v. *Ky. Distilleries Co.*, 255 U. S. 288, 292; *Eisner* v. *Macomber*, 252 U. S.

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* *Knowlton* v. *Moore*, 179 U. S. 41, 80; *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, 150; *Brushaber* v. *Union Pac. R. R.*, 240 U. S. 1, 19; *Eisner* v. *Macomber*, 252 U. S. 189, 205, 218.

189, 205). In the *Dawson* case, a Kentucky "license tax," on whiskey distillers or warehousemen with respect to whiskey withdrawn from bond or shipped in bond to a point outside the state, was held to be a *property* tax, and hence void, simply because an examination of the possible contingencies in which the tax would or would not become due (p. 293), led this Court to the conclusion that the thing *really taxed* was the *owner's right to take possession of his own property;* and that "to tax the right is to tax the value" (p. 294), saying,

> "To levy a tax *by reason of ownership* of property is to tax the property. Compare *Thompson* v. *Kreutzer,* 112 Miss. 165; *Thompson* v. *McLeod,* 112 Miss. 383. It can not be made an occupation or license tax *by calling* it so. See *Flint* v. *Stone Tracy Co.,* 220 U. S. 107, 148-150; *Zorme* v. *Minneapolis Syndicate,* 220 U. S. 187; *U. S.* v. *Emery, Bird, Thayer Realty Co.,* 237 U. S. 28."

Congress had the undoubted right to tax Mrs. Frick and Miss Frick upon their property interests in the policies. But such taxation would be a "direct" tax. As said in *Eisner* v. *Macomber,* 252 U. S. 189, 217

> "That Congress has power to tax shareholders *upon their property interests* in the stock of corporations is beyond question; and that such interests might be valued in view of the condition of the company, including its accumulated and undivided profits, is equally clear. But that this would be taxation of property *because of ownership,* and hence would require apportionment

> under the provisions of the Constitution, is settled beyond peradventure by previous decisions of this court.
>
> * * * neither under the Sixteenth Amendment nor otherwise has Congress power to tax without apportionment a true stock dividend made lawfully and in good faith, or the accumulated profits behind it, as income of the stockholder."

Bearing those settled principles in mind, let us examine the nature of the policies taxed, the ownership thereof, and the incidents of the taxation imposed thereon.

1. *The policies were the exclusive property of Mrs. Frick and Miss Frick.* Take the largest policy ($114,000) as a sample. In 1901, Mrs. Frick, being the owner of a prior paid-up policy, surrendered it to the Equitable Life Assurance Society and received in exchange a new policy, by which the insurance company unconditionally agreed to pay her $114,000 on the death of her husband. No premiums were paid on it. It was the absolute promise of the company to pay her $114,000 at her husband's death. That is personal property in its simplest form. It is property, just as a corporate bond, by which the Pennsylvania Railroad Company agrees to pay $1000 ninety-nine years from date, is personal property. That the maturity is in one instance fixed by the calendar and the other by the death of a third party is immaterial. The policy had a money value to Mrs. Frick. It could be borrowed on. It could be sold or "cashed in" for its surrender value. It was property included in the words "personal estate

or property" and would pass under that head by deed or will (*Elliott's Appeal,* 50 Pa. St. 75, 82; *Anderson's Appeal,* 85 Pa. St. 202,207; *Adams Express Co.* v. *Ohio,* 166 U. S. 185, 220, 222).

It was Mrs. Frick's property. Mr. Frick had no interest in or control over it. It was a direct contract between the insurance company and Mrs. Frick, whose vested interest was property of the most certain and valuable nature (*Entwistle* v. *Insurance Co.,* 202 Pa. 141, 143).

In order to relieve a wife and children as beneficiaries from the claims of creditors of an insolvent insured, Pennsylvania provided by statute, that life policies assigned to, or taken out in the name of, a wife or children, etc., shall be vested in them free from the claims of creditors of the insured even though the right to change the beneficiary was reserved by the insured or permitted by the company (Act April 15, 1868. P. L. 103, § 1; Act May 5, 1915, P. L. 253; Act May 17, 1919, P. L. 207, § 1; Digest Pa. Statute Law, §§ 12261-2; R. 34; see *Burlingham* v. *Crouse,* 228 U. S. 459, 472). The most satisfactory discussion of the nature of life insurance as property; the absolute ownership by the beneficiary of every element of property value therein; and the lack of property interest in the insured, will be found in the late case of *Tyler* v. *Treasurer & Receiver General,* 226 Mass. 306, no quotation from which will be given here, as such lengthy extracts appear in other Briefs filed herein.

There is a controlling case in this Court.

In *Washington Central Bank* v. *Hume,* 128 U. S. 195, 206, there was a contest between the creditors of an insolvent decedent, on the one hand, and his wife as beneficiary in a series of life insurance policies, on the other. The policies were taken, some before, others after, the insured's insolvency. This Court held that neither the insured's administrator nor his creditors could recover any part of the insurance or the premiums paid by the insured to keep his policies alive, saying:

> "We think it cannot be doubted that in the instance of contracts of insurance with a wife or children, or both, upon their insurable interest in the life of the husband or father, the latter, while they are living, can exercise no power of disposition over the same without their consent **nor has he any interest therein of which he can avail himself, nor upon his death have his personal representatives or his creditors any interest in the proceeds of such contracts which belong to the beneficiaries to whom they are payable.**
>
> It is indeed the general rule that a *policy,* and the *money* to become due under it, *belong, the moment it is issued,* to the person or persons *named in it as the beneficiary or beneficiaries,* and that there is no power in the person procuring the insurance by any act of his, by deed or by will, to transfer to any other person the interest of the person named. Bliss on Life Insurance, 2d ed. p. 517; *Glanz* v. *Gloeckler,* 10 Appellate Court Illinois, 484, per McAllister, J.; *S. C.* 104 Illinois, 573; *Wilburn* v. *Wilburn,* 83 Indiana, 55; *Ricker* v. *Charter Oak Ins. Co.,* 27 Minnesota, 193; *Charter Oak Life Ins. Co.* v. *Brant,* 47 Missouri, 419; *Gould* v. *Emerson,* 99 Mass. 154; *Knickerbocker Life Ins. Co.* v. *Weitz,* 99 Mass. 157.

This must ordinarily be so where the contract is directly with the beneficiary; in respect to policies running to the person insured, but payable to another having a direct pecuniary interest in the life insured; and where the proceeds are made to inure by positive statutory provisions. * * *

But, even though Hume paid this money out of his own funds when insolvent, and if such payment were within the statute of Elizabeth, this would not give the creditors any interest in the *proceeds* of the policies, which *belonged to the beneficiaries* for the reasons already stated.

Were the creditors, then, entitled to recover the premiums?

These premiums were paid by Hume to the insurance companies, and to recover from them would require proof that the latter participated in the alleged fraudulent intent, which is not claimed. Cases might be imagined of the payment of large premiums, out of all reasonable proportion to the known or reputed financial condition of the person paying, and under circumstances of grave suspicion, which might justify the inference of fraud on creditors in the withdrawal of such an amount from the debtor's resources; but no element of that sort exists here.

The premiums *form no part of the proceeds* of the policies, and cannot be deducted therefrom on that ground. * * *

This argument in the interest of creditors concedes that the debtor may rightfully preserve his family from suffering and want. It seems to us that the same public policy which justifies this, and recognizes the support of wife and children as a

positive obligation in law as well as morals, should be extended to protect them from destitution after the debtor's death, by permitting him, not to accumulate a fund as a permanent provision, but to devote a moderate portion of his earnings to keep on foot a security for support already, or which could thereby be, lawfully obtained, at least to the extent of requiring that, under such circumstances, the fraudulent intent of both parties to the transaction should be made out.

And inasmuch as there is no evidence from which such intent on the part of Mrs. Hume or the insurance companies could be inferred, in our judgment none of these premiums can be recovered."

That case (widely followed in the State courts, 14 Rose's Notes 2d Ed., 419; 1 Ann. Cases, 684, note) definitely determines that *from the moment the policies were issued,* they and the proceeds *thereof, belonged* solely to Mrs. Frick and Miss Frick; that any premiums paid by Mr. Frick *formed no part of the proceeds of the policies;* and that neither the insured, during his lifetime, nor his estate after his death, have any interest in or control over the policies or their proceeds (To the same effect, see *Lloyd* v. *Royal Union,* 245 Fed. 162, 165; *Halder* v. *Ins. Co.,* 77 S. C. 299; Cooley's Briefs on Insurance, Vol. 2, p. 1091, Vol. 4, pp. 3755-9, Vol. 6, p. 424, Vol. 7, p. 1568; *N. Y. Mutual Life* v. *Armstrong,* 117 U. S. 591). Indeed, it is because a life policy is property, a chose in action, that under some circumstances of fraud, the assignment of a policy by an insolvent debtor to his wife may be fol-

lowed and set aside under statutes against the transfer of property to cheat creditors (Ann. Cas., 1912 B, 896, note).

At Mr. Frick's death, the policies were property; they did not belong to him but to his wife and daughter, in whom title was vested. The property rights in the policies were absolute.

2. *The 25% tax is a "direct tax" imposed solely by reason of ownership.* Without restating the historical matter submitted at the hearing of the Income Tax Cases in 1895, it will be sufficient to refer to the briefs then filed and to the two opinions of CHIEF JUSTICE FULLER (157 U. S. 429; 158 U. S. 601) to demonstrate that the framers of the Constitution perfectly well understood the distinction between direct and indirect taxation; that taxes on property, real or personal, were direct taxes; that there was a great struggle over the grant of power to Congress to levy direct taxes, and that the rule of apportionment was the compromise by which the adoption of the Constitution was secured; that when the States surrendered certain great sources of revenue they retained that of direct taxation, and limited its concurrent grant to Congress; and that (158 U. S. 637)

> "taxes on personal property are likewise direct taxes."

Knowlton v. *Moore, Flint* v. *Stone Tracy Co.* and *Brushaber* v. *Union Pacific* reiterated that any tax levied on personal property *because of its ownership*

was a direct tax (178 U. S. 80, 82; 220 U. S. 150; 240 U. S. 19).

If Congress levies a 10% tax in respect of every corporate bond which matured and was paid to the holder, could that be called an "excise" tax? Would it not be a direct tax on the bonds?

The present tax on Mrs. Frick's $114,000 life insurance is imposed simply because she owns it.

If a 25% tax were imposed on $114,000 railroad bonds, or promissory notes, it would be conceded to be a direct tax.

If Mrs. Frick had a favorable contract, as for example a long lease on a building at Broad and Wall Streets, New York, for $50,000 a year rental (which could be sublet for say $200,000 a year), and Congress imposed a tax, not on the rental as income, but on the lease—no matter how its value were determined—the tax would be clearly direct.

Why is Mrs. Frick taxed except because of her ownership of the policies?

The phrase "direct tax" means something in the Constitution; the two separate provisions to prevent the levy of direct taxes save by apportionment, were intended to protect the individual from direct taxation by Congress.

The 25% tax imposed here is not on the manufacture, consumption or use of any article; it is not for any privilege exercised by Mrs. Frick except the privilege of *owning* property—and that privilege can not be taxed except by apportionment.

One might as well say that the Income Tax of 1894 was an excise or indirect tax, because it only taxed the *privilege* of a landlord of *receiving and collecting* his rent or of a capitalist of collecting coupons or dividends.

How could a tax be more direct than to take away 25% of the capital value of the property owned? It is neither more nor less than a capital levy on accumulated wealth.

For nearly twenty years Mrs. Frick held the *unconditional promise* of the insurance company to pay her $114,000 when her husband should die. That was a promise which had a definite marketable value; it could be sold at a discount from its face value based on her husband's age at any given moment. On its maturity, the United States asserts the right to take by taxation 25% thereof. If that is not a direct tax on property, what is it? Suppose Mrs. Frick had in 1915 sold it for say $95,000 to A. In 1919 when A collected $114,000, he could be taxed on the $19,000 profit because of the 16th Amendment; but must he also pay 25% tax on the original $95,000 or on the $114,000? What would that be save a direct tax?

During Mr. Frick's lifetime, that policy in his wife's ownership might have been subjected to an *ad valorem* tax by the State of her domicile. Why? Because it was *property,* capable of sale or pledge. As aptly said in *Adams Express Co.* v. *Ohio,* 166 U. S. 171, 220, 225, in order to sustain the right of the State to tax the value resulting from a unity of use,

> "Courts must recognize things as they are and as possessing a value which is accorded to them

in the markets of the world * * * whatever property is worth for the purposes of income and sale it is also worth for purposes of taxation."

That which has value and is taxed by Congress because, and solely because, it represents property, must be taxed by apportionment.

There are today about sixty billion dollars ($60,000,000,000) of outstanding life insurance in this country, to secure the payment of which at maturity about ten billion dollars ($10,000,000,000) of assets has been accumulated. Those policies are property whether before or after the death of the insured, which event only fixes the maturity of the obligation.

If Congress should levy a tax of say 1% or 5% or 10% on the face amount of all policies held by all the policyholders of this country—the tax to be paid by the insurance companies out of the policies' reserves—could it be said that such a tax was an excise or indirect tax? Could it be said to be a tax for the privilege of holding insurance? Would it be other than a direct tax, pure and simple?

Should the courts, whose duty is to protect the individual from the encroachments of Government, seek to find ways to hold taxes indirect, when by any canon applicable to any other situation they would be clearly direct?

SECOND POINT.

The 25% tax imposed on beneficiaries' life insurance is neither a death duty nor a succession tax as those terms are defined in *Scholey* v. *Rew, Knowlton* v. *Moore, New York Trust Co.* v. *Eisner* or in any other decision of this court; and hence this tax cannot be sustained as an "excise" tax on the authority of those cases.

1. *The 25% tax is not an "excise" within any definition ever suggested by this Court.* In many cases, some of which are cited in the margin*, this Court has discussed what constitutes an "excise" tax; and it has considered, and to a considerable extent cited, a mass of historical data and definitions on the subject. The result is that whether we consider (*a*) the *articles* on which excises was imposed in 1787 in Great Britain or her colonies, (*b*) the *definitions* by ancient or modern lexicographers, (*c*) the nature of the tax as judicially determined, or (*d*) all of them combined, no support can be found for considering as an "excise", a tax imposed on property which a person has acquired years before, which property is not being used in any particular way, but *merely owned.*

If the distinction formulated in the *Pollock* case (157 U. S., at p. 558) that taxes which can be shifted upon another are indirect, while those which can not be avoided are direct, is disputed (*Knowlton* v. *Moore,* 178

* *Pollock* cases, 157 U. S. 429; 158 U. S. 601; *Knowlton* v. *Moore,* 178 U. S. 41; *Patton* v. *Brady,* 184 U. S. 608, 617; *Thomas* v. *U. S.,* 192 U. S. 363; *Spreckels Sugar Refining Co.* v. *McClain,* Id. 397; *Flint* v. *Stone Tracy Co.,* 220 U. S. 107, 150-1; *Billings* v. *U. S.,* 232 U. S. 261.

U. S. at p. 62), still this Court has never gone further than to say that "excises" are taxes on (1) the consumption, manufacture, sale and use of certain commodities and articles, (2) the exercise of certain privileges, (3) particular transactions, vocations, occupations and the like, and (4) those subjects historically recognized as the antithesis of direct taxes.

Judged by any definition heretofore given, the present tax on Mrs. Frick's policy can not be sustained, and even the Government so concedes, except to insist that it may be sustained as a death duty or succession tax.

Bearing in mind that no property passed from the dead [Frick] to the living [Mrs. Frick] either by will, intestacy, or power of appointment conferred by Frick, let us examine the cases in which death duties have been held to be excises, *i. e.*, indirect taxes.

2. In every inheritance tax case that has ever reached this Court, whether involving a State or Federal statute, the tax has been with respect of an estate that passed *from* the dead *to* the living, *i. e.*, an estate that *belonged* to A and passed from him to a beneficiary either (1) at A's death by intestacy, will or trust deed to take effect upon his own death, or (2) at the death of B, pursuant to some power of appointment conferred by A on B to take effect at B's death, and exercised by B, which exercise by B this Court held was the cause of the transfer of the estate from the dead to the living.

In short, the tax was imposed upon the artificial right or privilege given by the law to A to control (either directly by his own act, automatically by intestacy, or indirectly by the act of some donee of his power) what should become of his assets after he died.

An entirely different situation is presented in this case. The tax here contested is not imposed with respect of any estate of Mr. Frick passing on his death, by either will, deed, power of appointment, or the intestate laws of the State. It is in respect of a personal contract—property—between two living third parties. The subject of the tax [the policies] *never belonged to* Mr. Frick. They never *passed from* him.

DECISIONS OF THIS COURT.

1. *The effect of this Court's decisions.* At the risk of some repetition, it must be emphasized that a review of *every case* in this Court on the subject, establishes the following propositions, which, unless now radically extended by a new decision, exempt the Frick policies from inheritance taxation.

First: The inheritance tax—whether a legacy tax as in the 1898 Act or a net estate tax in the 1918 Act—was held to be an "excise" solely because it was imposed upon *the interest of the decedent* which *ceased* by reason of death and thereupon *passed to a beneficiary*—from the dead to the living.

N. B.: But here, (*a*) the decedent (Frick) had no interest which could or did cease at death, and (*b*) no

interest passed to any beneficiary, as they already owned the policies absolutely.

Second: The property with respect of which the tax is imposed, must be *property of the decedent,* who directed its disposition after his own death either (1) by intestacy, will, or deed to take effect at death or (2) by conferring a power of appointment on another to dispose of it at such other's death.

N. B.: None of those conditions exist here, as the property never was Frick's, and he neither disposed of it nor authorized another to dispose of it.

There must be *ownership* by the *decedent,* or exercise by the decedent of the power of ownership (*i. e.,* exercise of a power of appointment) resulting in a *cessation* of his interest and a transfer to another, in order to sustain an inheritance tax as an "excise".

Third: The sole basis of sustaining such taxes as "excises" is that there is no inherent right in A to direct the disposition of his property after his death; and that as the State alone authorizes or protects such disposition, it can attach to such privilege any conditions it chooses—and the Federal tax is simply imposed on the exercise of the privilege.

N. B.: Here, no privilege is granted by the State A contract to pay money is merely *performed;* and a tax on the inherent and essential element of ownership, *i. e.,* the right to take possession of one's own property, is a tax on property (*Dawson* v. *Kentucky Distilleries Co.,* 255 U. S. 288, 294).

If, for example, in the *Dawson* case the whiskey warehouseman had by his warehouse receipt agreed to store the whiskey so long as he lived, but at his death the owner must remove it, the 50 cent a gallon tax could never have been sustained as an excise tax, because, forsooth, death *caused* the owner to take possession of his own whiskey and remove it from the warehouse.

2. *Cases involving Federal Inheritance Tax Laws.* In *Scholey* v. *Rew,* 23 Wall. 331, a tax in respect of any disposition of real estate by will, deed or laws of descent, to become effective upon death, was held to be a tax on the right to become the successor of real estate on the death of the person whose interest is acquired, to wit: an excise tax on the devolution of the title, and not a direct tax.

Although the *reasoning* by which that result was reached (pp. 347-8) was squarely rejected in the *Pollock* cases, and the case was thought to be overruled, yet *Knowlton* v. *Moore,* 178 U. S. 41, 79, 81, held that the *decision* in *Scholey* v. *Rew, i. e.,* that a succession tax is an excise tax, was left unaffected.

Knowlton v. Moore, 178 U. S. 41.

In 1899 the 16th Amendment had not been adopted; the *Pollock* cases were the law; four of the majority justices in the *Pollock* cases remained (Fuller, Gray, Brewer, Shiras) while but three of the dissenting justices were left (Harlan, Brown, White); one of the majority (Field) and one of the minority (Jackson) were dead; two new justices had come on the court (Peckham and McKenna); but Peckham took no part in the decision of *Knowlton* v. *Moore,* so that of the eight justices, who decided the case, at least four were committed to the doctrine that a tax on income was a direct tax, even assuming that the three dissenting justices refused to be bound by the *Pollock* case and that McKenna should unite with them;

The 1898 Inheritance Tax law was a tax not on the net estate, but on the *legacy* or *distributive shares* of personal property only. If it had been construed as a tax on the *receipt* of the legacy or share it would have been a tax on income, and void as a direct tax under the *Pollock* case. Therefore, in order at that time to sustain the tax at all, it had to be construed as a death duty, not on the estate *qua* estate, nor on the legacy or share as such, nor on the receipt by the beneficiary of the legacy, but on the *cessation of the decedent's interest.*

Only by an understanding of the judicial history of the times, can one appreciate the reason for the peculiar and refined basis on which the right to levy an inherit-

ance tax, without apportionment, was rested. That explains the consistent holding in all subsequent cases that, so far as the Federal Government is concerned, the basis of its power to levy an "excise" death duty rests on the right to tax the interest *which ceased by death*—not the interest that was *acquired* by death—for the latter would be *income* or capital—and a tax thereon would necessarily be a "direct" tax.

In *Knowlton* v. *Moore,* it was held on full consideration:

I. That under the practice of many nations some form of death duty was a well known method of taxation, whether called probate or stamp duty, legacy or estate tax, etc.; that in all countries such taxes (p. 56)

> "rest in their essence upon the principle that death is the generating source from which the particular taxing power takes its being, and that it is the *power to transmit,* or the transmission *from the dead to the living,* on which such taxes are more immediately rested";

and that under the broad power "to lay and collect taxes, duties, imports and excises," Congress could levy the tax commonly called an inheritance tax (pp. 47-61).

II. That generally speaking, such death duties have in all countries been considered as *different* from taxes levied on real or personal property by reason of the ownership or possession thereof; and that Congress had, in the legislation of 1797, 1862-1866, 1894, treated death duties as indirect taxes (p. 78).

III. That *Scholey* v. *Rew* was not overruled by the *Pollock* cases; and, hence, an inheritance tax, by virtue

of that decision, (apparently on the doctrine of *stare decisis*), must be deemed an excise tax, and *not* a direct tax.

However unsatisfactory to a logical mind, the *tour de force* may be, by which the last conclusion was reached (p. 42 note, *infra*), it is now settled that an inheritance tax is an excise tax.

But it is important to note the *precise nature* of the grounds on which the tax was held to be an excise tax:

(p. 47):

"Taxes of this general character are universally deemed to relate, not to property *eo nomine,* but to its passage *by will or by descent* in cases of intestacy, as distinguished from taxes imposed on property, real or personal, as such, because of its ownership and possession. In other words, the public contribution which death duties exact is predicated on the *passing of property as the result of death,* as distinct from a tax on property disassociated from its transmission or receipt by will, or as the result of intestacy."

(p. 51):

"Thus it came to pass that the system of death duties prevailing in England and that adopted by Congress—leaving out of view the differences in rates and the administrative provisions—were substantially identical, and of a threefold nature, that is, (1) a probate duty charged upon the *whole estate,* (2) a legacy duty charged upon each *legacy* or *distributive share* of personalty, and (3) a succession duty charged against *each interest in real property.*"

(p. 56):

"Thus, looking over the whole field, and considering death duties in the order in which we have reviewed them, that is, in the Roman and ancient law, in that of modern France, Germany and other continental countries, in England and those of her colonies where such laws have been enacted, in the legislation of the United States and the several States of the Union, the following appears: Although different modes of assessing such duties prevail, and although they have different accidental names, such as probate duties, stamp duties, taxes on the transaction, or the act of passing of an estate or a succession, legacy taxes, estate taxes or privilege taxes, nevertheless tax laws of this nature in all countries rest in their essence upon the principle that *death* is the generating source from which the particular taxing power takes its being and that it is the *power to transmit*, or the *transmission from the dead to the living*, on which such taxes are more immediately rested."

(p. 57):

"Confusion of thought may arise unless it be always remembered that, fundamentally considered, it is *the power to transmit or the transmission or receipt of property by death* which is the subject levied upon by all death duties".

(p. 59):

"The thing forming the universal subject of taxation upon which inheritance and legacy taxes rest is the *transmission or receipt*, and not the right existing to regulate". (p. 59).

In *Hertz* v. *Woodman,* 218 U. S. 205, 219, the subject of the tax was thus stated:

> "Now, *what is* the property, right or thing which is made subject to the tax? This has been most conclusively answered by *Knowlton* v. *Moore,* 178 U. S. 41, 56, where the section in question is construed as laying a tax upon the *transmission,* or *the right to succeed to a legacy,* or *distributive share or gift in contemplation of death,* passing after the act. * * *
>
> "To repeat then: The subject of the tax or duty exacted by § 29 is the *right of succession which passes by death* to a vested beneficial right of possession or enjoyment to a *legacy* or *distributive share.*"

In *New York Trust Co.* v. *Eisner,* 256 U. S. 345, 349 the 1916 Act taxing net assets of the estate was sustained as an excise tax; the Court saying, with respect to the attempted distinction between a tax on the privilege of bequeathing and privilege of receiving;

> "But that matter also is disposed of by *Knowlton* v. *Moore,* not by an attempt to make some scientific distinction, which would be at least difficult, but on an interpretation of language by its traditional use—on *the practical and historical ground that this kind of tax always has been regarded as the antithesis of a direct tax;* 'has ever been treated as a duty or excise, because of the particular occasion which gives rise to its levy.' 178 U. S. 81-83. Upon this point a page of history is worth a volume of logic."

But there is no practical or historical basis for holding that a tax, such as the 25% tax on life insurance

beneficiaries, has ever, at any time, or in any country, been deemed an indirect tax. It is a completely novel and radical departure from all former death duties. It seeks to reach accumulated wealth of third persons—which is not and never has been the estate of the decedent.

In *Y. M. C. A.* v. *Davis,* 264 U. S. 47, 50, it was said of the 1918 Act, here involved,

> "What was being imposed here was an excise upon the transfer of an estate *upon death of the owner.* It was not a tax upon succession and receipt of benefits under the law or the will. It was death duties as distinguished from a legacy or succession tax. What this law taxes is not the interest to which the legatees and devisees succeeded on death, but *the interest which ceased by reason of the death. Knowlton* v. *Moore,* 178 U. S. 41, 48, 49".

That is a clear and unmistakable declaration that what the 1918 Act actually did [irrespective of what Congress might do] was to tax the transfer of the *owner's* (Frick's) estate, to-wit, *his* interest which ceased at *his* death. But Frick had no ownership nor interest in the policies. There was no transfer of anything he owned; he had no interest which ceased at his death. On the other hand, the owners have not died.

In *Edwards* v. *Slocum,* 264 U. S. 61, 62, it is said of the same Act:

> "But this is not a tax upon a residue. It is a tax upon a transfer *of his net estate by a decedent,*

a distinction marked by the words that we have quoted from the statute, and previously commented upon at length in *Knowlton* v. *Moore,* 178 U. S. 41, 49, 77. It comes into existence before and is independent of the receipt of the property by the legatee. It taxes, as Hanson, Death Duties, puts it in a passage cited in 178 U. S. 49, 'not the interest to which some person succeeds on a death, but *the interest which ceased by reason of the death.*' It levies a sum equal to a certain percentage of the value of the net estate, and provides the criteria by which the net estate shall be ascertained."

There again, it is declared that the thing taxed is the decedent's transfer of *his own* estate, *i. e.,* his interest which ceased at his death. By that rule the 1918 Act has nothing to operate on with respect to the policies owned by the wife and daughter.

All other decisions under the 1898, 1916 and 1918 Acts are summarized in the margin,* but as they re-

* Under the 1898 Act, it was held that the tax applied to a legacy to a city (*Snyder* v. *Bettman,* 190 U. S. 249), but that while Congress had the power, it had not in fact used language to tax intangible personal property in this country belonging to an alien abroad and which passed by foreign laws to another alien abroad (*Eidman* v. *Martinez,* 184 U. S. 578); that residuary interests were not taxable until the time when they came into possession or enjoyment (*Vanderbilt* v. *Eidman,* 196 U. S. 480); that the tax became "imposed" at the time of death which vested the right to immediate possession or enjoyment and was not remitted by the repealing Act of 1902 (*Hertz* v. *Woodman,* 218 U. S. 205) but where under the State Court construction of the will the beneficial interest did not vest until after July 1, 1902, the tax was repealed as to such interests (*Uterhart* v. *United States,* 240 U. S. 598).

Under the 1916 Act, although Congress had the power to tax, it did not in fact tax property disposed of by a power of

late rather to details of application or construction, it is needless to review them, except to repeat that wherever the tax was sustained, it was a case of the decedent's *own* estate being transferred by will or intestate laws.

2. *Cases involving State inheritance tax laws.* Cases involving State succession taxes might well be laid aside as irrelevant, because of the differences (*a*) in the sources of the power from which they spring, and (*b*) in the constitutional limitations imposed thereon, from those governing Federal taxation (*Pollock* case, 157 U. S. 429, 578; *Knowlton* v. *Moore,* 178 U. S. 41, 57, 58; *Chanler* v. *Kelsey,* 205 U. S. 466, 480; *Snyder* v. *Bettman,* 190 U. S. 249, 256).

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appointment created before the Act but executed after the Act (*U. S.* v. *Field,* 255 U. S. 257); nor did it apply to property which, before the Act, had been conveyed, in trust, for life with remainders over (*Schwab* v. *Doyle,* 258 U. S. 529) nor to transfer in contemplation of death if made before its passage (*Union Trust Co.* v. *Wardell,* 258 U. S. 537; *Levy* v. *Wardell, Id.* 542); and the tax could be imposed on the value of the Estate even though it was in part composed of State bonds (*Greiner* v. *Lewellyn,* 258 U. S. 384).

Under the 1918 Act, Federal inheritance taxes are to be paid out of the estate generally, and charitable residuary legatees only get what is left after the payment of taxes, debts and specific gifts in full; and the fact that the Act authorizes the deduction of charitable bequests from the gross estate in order to determine the net taxable estate, does not authorize the residuary charitable legatees to shift the payment of the inheritance tax upon the specific gifts so as to increase the size of the residuary estate (*Y. M. C. A.* v. *Davis,* 264 U. S. 47); and the amount taxable is only the net estate left after deducting debts, expenses and charitable bequests, including residuary charitable bequests; and the tax paid out of the exempt residuary estate (*Y. M. C. A.* v. *Davis, supra*) upon the taxable net estate, can not in turn be added to such taxable net estate so as to require a further payment of a tax *on* the tax (*Edwards* v. *Slocum,* 264 U. S. 61, 62).

As the States began to adopt inheritance tax laws, most of them took the plain form of a direct percentage tax upon the value either of (1) the decedent's estate, or (2) the legacies and devises, or, (3) in case of intestacy, the shares of the heirs.

Apparently such taxes were, as the language plainly imported, nothing but *direct property taxes,* and consequently, subject to all State constitutional limitations on *property* taxation. So as to avoid the local constitutional requirements of uniformity, equality, etc., the State courts quickly *invented the pure legal fiction* that inheritance taxes (no matter what the language nor how specifically the tax was imposed on the *property* left by the decedent) were *not* taxes on *property,* but were taxes upon the *privilege* of succeeding to the inheritance or becoming a beneficiary under the will, such privilege being a right created by the State* and, therefore, taxable by it without regard to restrictions on *property* taxation.

When, on appeal to this Court, those statutes were attacked, (generally) as in violation of the "due process" and "equal protection" clauses of the 14th Amendment, the construction of them by the State Courts as "succession" taxes and *not* property taxes was, of course, binding here, was accepted as authoritative under the State laws, and greatly limited the scope of the inquiry by this Court. In every instance the attack on the State law has failed here, and the cases cited in the margin illustrate the extent to which

*1 Ann. Cases 30 note; *Rodman* v. *Com.,* 130 Ky. 88; 33 L. R. A. (N. S.) 592 note; 37 Cyc. 1553; 11 Encyl., Sup. Ct. Rep. 289.

this Court has sustained the power of the State to reach many kinds of property interests by means of inheritance taxes.* But they are wholly irrelevant as to

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* *Mager* v. *Grima,* 8 How. 490 (tax on a legacy to a non-resident alien sister *held* not to be a tax on exports or a regulation of commerce, and to be within power of State to regulate an alien's capacity to take property within the State); *Carpenter* v. *Pennsylvania,* 17 How. 456 (tax on a citizen's estate, even though part is outside the state, was sustained as within power of State over transfer of decedent's property); *U. S.* v. *Perkins,* 163 U. S. 625 (tax on all property passing by will *held* to apply to a devise and bequest to the United States, as the tax was imposed before the property reached the United States); *Magoun* v. *Illinois T. & S. B.,* 170 U. S. 283 (tax on all property passing by will or intestacy, the rate varying according to the consanguinity of the beneficiary, and increasing progressively when the beneficiaries were strangers or distant relatives, *held* to be a succession tax and not to violate the equal protection clause of the 14th Amendment, but to be a legitimate classification of taxation); *Plummer* v. *Coler,* 178 U. S. 115 (tax on a legacy *held* to apply to a legacy of U. S. bonds (which by statute were exempt from taxation) because not a tax on property but on the privilege of taking property by will, measured by the value of the legacy, and not to be a tax on a Federal instrumentality, but deducted before the legacy reached the beneficiary); *Orr* v. *Gilman,* 183 U. S. 278 (tax upon the exercise by will after the statute of a power of appointment conferred by will before the statute, *held,* in accordance with the New York rule, not to be a tax on property but on the privilege of exercising a power of appointment; and *held* not to violate the contract clause nor the 14th Amendment, even though part of the property passing under the power was tax exempt bonds); *Blackstone* v. *Miller,* 188 U. S. 189 (14th Amendment did not forbid New York Inheritance tax on money belonging to Illinois decedent, but left on deposit for over a year in New York); *Campbell* v. *California,* 200 U. S. 87 (equal protection clause did not forbid California from imposing inheritance tax on legacies to brothers and sisters and exempting sons-in-law and daughters-in-law—a legitimate classification); *Cahen* v. *Brewster,* 203 U. S. 543 (tax on estates of persons dying before the Act but still undistributed, *held* not to violate "due process" clause, as State could exercise power to tax privilege up to time legatee actually received the property); *Board of Education* v. *Illinois,* 203 U. S. 553 (not a denial of equal protection of laws for a State to exempt domestic charities from inheritance tax while leaving foreign charitable corporations subject thereto); *Chanler* v. *Kelsey,* 205 U. S. 466 (the State court ruling that life estate coupled with a power to dis-

whether under the Federal Constitution, they are *direct* taxes or excises.

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pose of remainder, conferred by deed before the Act, when exercised by will after the Act, taxable as a transfer of remainder because the beneficiary took by the power and not from the original grantor, *held* not to violate either the due process or contract clauses); *Beers* v. *Glynn*, 211 U. S. 477 (no violation of due process or equal protection clauses by New York inheritance tax law which taxed personalty of non-resident decedents owning real estate in New York and did not tax non-resident's personalty if he owned no real estate in State—a permissible exemption); *Moffitt* v. *Kelly*, 218 U. S. 400 (a wife's vested right in community property may be taxed without violating the contract or equal protection clauses); *Keeney* v. *New York*, 222 U. S. 525, *held* the Act sustained in *Plummer* v. *Coler*, 178 U. S. 115, to justify a tax upon a transfer *inter vivos* to a trustee to hold for grantor's life and at her death to pay income to her children, because by the State decisions it was not a property tax but one on transfers to take effect in enjoyment at grantor's death and hence not a violation of the 14th Amendment, as State can tax privilege of creating or succeeding to artificial estates with limitations over); *Wheeler* v. *New York*, 233 U. S. 434 (tax sustained on non-resident's property in State consisting of notes executed by non-resident makers, as not violating due process clause); *Bullen* v. *Wisconsin*, 240 U. S. 625 (tax sustained with respect of property conveyed by trust deed to foreign trustee, reserving power of control during donor's life and at his death to go as he might appoint, etc.); *Petersen* v. *Iowa*, 245 U. S. 170; *Duus* v. *Brown*, Id. 176 (taxes on legacies to non-resident aliens at a higher rate than to residents are not violative of Denmark treaty); *Maxwell* v. *Bugbee*, 250 U. S. 519 (by 5 to 4 decision, *held* that taxing property in the State belonging to non-residents was valid under the privileges and immunities, equal protection and due process clauses, even though its effect was to impose a greater tax than would have resulted on equal amount of property if decedent had been a resident); *Watson* v. *State Comptroller*, 254 U. S. 122, and *Bankers Trust Co.* v. *Blodgett*, 260 U. S. 647 (acts sustained which imposed an additional inheritance tax with respect of the transfer of property on which taxes had not been paid during the owner's life time, as not violating the due process, equal protection or *ex post facto* clauses); *Nickel* v. *Cole*, 256 U. S. 222 (remainder interests under a will and deed for benefit of grantor for life held taxable as transfer to take effect at death, even though State court gave wrong reason for its decision).

It will be noted that wherever a State statute was sustained as an inheritance tax, the property always *belonged* to the decedent and (1) passed at his death to his heirs or legatees or (2) passed by trust deed or power of appointment on the death of the grantor (or a third party named by the grantor)—so that in each instance the transfer, *i. e.,* possession and enjoyment of the estate, took effect at, and by reason of, the death of *the grantor or person exercising the power of appointment.* Such cases lend no support to the proposition whether that a tax on life insurance policies held by third persons is an "excise" tax.

REPLY TO THE GOVERNMENT'S CONTENTIONS.

The Government concedes, as it must, that, at Frick's death, *no privilege,* granted by the State, *was exercised* as to the insurance; and that *no money* passed from the *dead* to the living; but it insists that as (say) $114,000 passed from the Equitable Life to Mrs. Frick in fulfillment of a promise to pay money, such a passage of money from the living to the living is a proper subject of an excise tax, because Frick's death fixed the moment of time when the insurance company became legally bound to pay to Mrs. Frick what it had promised, 18 years before, to pay to her.

The Government seeks to strengthen its position by an argument substantially as follows:

I. The act of a policyholder in taking out (or permitting his wife, child, or creditor to take out, Cf. Revenue Act of 1924, §   ) a policy payable to such wife, child or creditor, is a *quasi*-testamentary act* and hence when Mr. Frick died, Mrs. Frick merely came into possession and enjoyment of an estate which Mr. Frick had, while alive, *transferred to take effect at his death;* and that property so acquired is subject to a death duty.

II. That the decisions of this Court sustain such a view of the nature of (*a*) life insurance, and (*b*) death duties.

The fallacy in the Government's position lies in the fact that (*a*) life insurance policies are personal contracts, are not *quasi*-testamentary in character, and bear no analogy to the transactions cited, (*b*) the decisions of this Court on the nature of the death duties that can be imposed as "excises", do not justify, and are totally inconsistent with the validity of the 25% tax on beneficiaries' insurance, and (*c*) the only ground on which inheritance taxes can be sustained as "excises", is the decision in *Knowlton* v. *Moore,* where the nature of such taxes is defined, and by which definition the

* Analogous to a *donatio causa mortis* or to a deed of trust conveying a life estate to A (or reserving a life estate to the grantor *Keeney* v. *New York,* 222 U. S. 525; *Bullen* v. *Wisconsin,* 240 U. S. 625; *Nickel* v. *Cole,* 256 U. S. 222), with power of appointment in A to dispose of the remainder on the death of the grantor (*Keeney,* *Bullen* and *Nickel* cases) or on death of A (*Orr* v. *Gilman,* 183 U. S. 278; *Chanler* v. *Kelsey,* 205 U. S. 466).

Government is concluded and the present 25% tax is condemned* (pp. 30-32, *supra*).

Let us analyze the conceptions involved in that argument. We submit:

(1) *Life insurance is not testamentary in character, but it is a personal contract of indemnity against loss.* There is not a suggestion in the literature of the law that a life policy between a company and a beneficiary, or indeed any insurance policy, is *quasi*-testamentary in its nature.

The Courts have repeatedly held that the disposition of life insurance was *not* testamentary in character; that insurance payable to beneficiaries is not a part of the insured's estate nor be subject to an inheritance tax (See the excellent discussion in *Re Voorhees Estate,* 193 N. Y. Sup. 168, 172; *Re Parsons' Estate,* 102 N. Y. Sup. 168; *Tyler* v. *Treasurer, etc.,* 226 Mass. 306).

In *N. Y. Life Ins. Co.* v. *Deer Lodge,* 231 U. S. 495, 508, it was held after elaborate consideration

> "A policy of insurance, the cases declare, is a *personal contract, a mere indemnity,* for a con-

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*It is interesting to note (*Cf.* 29, *supra*) that the holding in *Knowlton* v. *Moore,* 178 U. S. 41, that an inheritance tax is an excise, and not a direct tax, is based on three points, to wit: (*a*) that Congress had always treated death duties as excises (p. 78)—but so it had treated ten income tax laws until the *Pollock* cases; (*b*) that *Scholey* v. *Rew,* 23 Wall. 331, holding succession taxes to be excises, was still the law, and had *not* been overruled by the *Pollock* cases (pp. 78-81)—although concededly the *reasons* advanced in *Scholey* v. *Rew* for its holding, *were* overruled in the *Pollock* cases; and (*c*) that the *Pollock* cases did not decide—what they plainly said—about the definition of indirect taxes (p. 82).

The decision in *Knowlton* v. *Moore* was a *tour de force,* of great simplicity, resting (despite its 67 pages of opinion) on the simple *declaration* (p 83) that the tax was not direct, but an excise, and that *Scholey v. Rew,* had so decided and had not been overruled (p. 78).

Some of the interesting unwritten history of this Court revolves around this opinion by a dissenting Justice in the *Pollock* cases, who, to the end, claimed that the *Pollock* cases were based on a "mistaken theory" (*Stanton* v. *Baltic Mining Co.,* 240 U. S. at p. 113).

sideration, against the happening of some contingent event, which may bring detriment to life or property, and *its character is the same no matter what the event insured against,* whether fire or hurricane, acts of man or acts of God, storms on land or storms on sea, *death* or lesser accident."

In *U. S.* v. *Supplee-Biddle Co.,* 265 U. S. 189, 195, it is said:

> "Life insurance in such a case is like that of fire and marine insurance, *a contract of indemnity. Central Bank of Washington* v. *Hume,* 128 U. S. 195. The benefit to be gained by death has no periodicity. *It is a substitution of money value for something permanently lost* either in a house, a ship, or a *life.*"

In *Central Bank of Washington* v. *Hume,* 128 U. S. 195, 205, it is said:

> "Marine and fire insurance is considered as *strictly* an indemnity; but while this is not so as to life insurance, which is simply a contract, so far as the company is concerned, to pay a certain sum of money upon the occurrence of an event which is sure at some time to happen, in consideration of the payment of the premiums as stipulated, nevertheless the contract is *also a contract of indemnity.*"

Indeed, as to the $114,000 policy, Mr. Frick paid no premiums on it, had no rights in it or control over any feature of it; and it was an unconditional promise, made in 1901, to pay $114,000 flat to Mrs. Frick on the death of her husband. It was in substance a promissory note payable at a third party's death.

Insurance policies are not testamentary in any sense whatever because (*a*) they do not comply with the

Statutory requirements as to wills, (*b*) they are not gifts in contemplation of death, as they can only be secured by persons who are in good health and not in contemplation of death, and they are not *gifts* at all, but *independent contracts* between the company and the beneficiary.

The Government disregards the repeated statements of this Court that the thing taxed is *the interest that ceased by death;* and it insists that the thing taxed is *the enjoyment or possession of anything* that, in some way, comes to be enjoyed or possessed by reason of a death. According to that theory, if A devised a life estate to B with remainder to C, there could be, *first,* an excise tax on all A's estate because his interest ceased at his death, and, *second,* another excise tax at B's death, because C came into enjoyment or possession on the occasion of a death, *i. e.,* B's. No such claim has ever been sustained in any case.

All the Government's contentions are reducible to this: Life insurance is a means by which the insured accumulates wealth; and the assignment of a policy to a wife, or its original issuance to her as the beneficiary thereof, is a gift or transfer in contemplation of death, of which gift such beneficiary only secures the enjoyment or possession at the donor's death, and hence it is subject to an excise tax.

Such an argument must be promptly rejected for various reasons:

1. An insurance policy is an *indemnity contract* between a company and the beneficiary, with which the

insured (unless his estate is the beneficiary) is ordinarily not concerned. He can pay the premiums or not as he pleases. His life is merely the *subject* of the contract between the company and the beneficiary. He is in no sense the donor of any rights or interests.

2. A simple illustration will be enlightening: If a man dies after paying (say) one premium, and his wife as beneficiary collects $100,000. insurance, how can it be said that the insured *accumulated* $100,000. or *transferred* it to his wife, etc. The wife was merely indemnified by the company for the monetary loss sustained by husband's death, exactly as she might have been indemnified for the loss of a jewel or against theft by a burglar.

The Government's argument reveals a fatal misconception of the nature of life insurance.

3. When a man takes out (or subsequently assigns) a policy in favor of his wife, daughter or creditor, that act is *not* a gift to take effect in enjoyment or possession at his death, as those phrases have been used in dealing with transfers by deed of a grantor's estate, reserving the use for life to himself and giving the remainder to take effect at his death.

The gift (if it can be called a gift at all) of the policy is *completed* when the beneficiary's name is written in the policy and it is delivered to her. She has then, immediately, the full ownership, possession and enjoyment of the donor's *gift, i. e.,* the policy. Whether she

ever gets the *indemnity* provided in the contract is another matter entirely, and in some cases depends on whether the insured or she elects to pay the future premiums. The point is that so far as the donor's so-called *gift or transfer* is concerned, it is not one where the enjoyment is *postponed* until his death, but the full enjoyment of the gift, *qua* gift, is in *præsenti* (*Girard Trust Co.* v. *McCaughn, Collector,* Feb. 4, 1924, reprinted in Appendix to Mr. Gordon's Brief). The beneficiary can at once sell or assign the policy to a third party who then owns absolutely the property (policy) and the original beneficiary has no possible further interest.

4. In *Penn Mutual Co.* v. *Lederer,* 252 U. S. 523, there are some expressions *arguendo* (and wholly unnecessary to sustain the correctness of that decision) to the effect that mutual life insurance "is largely that of savings investment" (p. 531) and an analogy is drawn between the deposit of savings in a bank and the payment of premiums by a policy holder. From those inaccurate expressions, the Government argues that a life insurance policy is the same as if a depositor had assigned his savings account to his wife to be her's on his death. There is no analogy whatever. In the savings bank case, the deposit (and the interest earned thereon) is a chose in action, and the retention of the title in the depositor during life, the deposit going to his wife at his death, is a plain transmission of the decedent's interest (which ceased at death) to his wife, and subject

to an excise tax under the express language of *Knowlton* v. *Moore* and the cases following it.

But life insurance is primarily for *protection.* The supposed savings feature is wholly incidental, arises from the natu of "level" premium insurance, and is a comparatively small part of the subject.

Instead of a man paying each year the premium based on the mathematical probability of his death during the year, very low at first and increasing slowly for many years, and then by leaps and bounds rising to prohibitive figures, so that in old age he would pay almost the full face of the policy each year, it was long ago discovered that, by a simple arithmetical calculation of interest and discount, exactly the same result could be reached by the man paying the same sum each year.

Protection, i. e., indemnity, is the fundamental and only object of life insurance. The so-called dividends are *necessary* excess payments in order to furnish a factor of safety and are regularly returned. The Reserve is not a "savings" at all. It is the mathematical sum necessary to be held to enable the Company, year by year, to pay its death losses. The moment it is impaired *one dollar* the company is insolvent.

The so-called "savings" feature is not a saving by the policyholder. It is the sum he pays for *protection,* and its temporary accumulation is merely what he pays for the advantage of not being compelled in old age suddenly to pay enormous sums each year for the current year's protection cost. In short, he pays *in*

advance for a part of that *future* protection if he happens to live to old age.

Life insurance payable to a beneficiary (other than the man's own estate) is not an accumulation of an estate by a man (in which at his death his interest ceases, and which is taxable by an "indirect" tax), but it is a contract of indemnity by which the company indemnifies the beneficiary against loss by death; and the decedent may or may not spend his income during life in furnishing such indemnity. But when he dies, *he* has no interest that ceases, and there is nothing on which the inheritance tax, as defined in *Knowlton* v. *Moore* and permitted as an *excise,* can operate.

2. *The decisions of this Court do not sustain the Government's view of either life insurance or death duties.* In view of what has already been shown, it is enough to refer to *Central Bank of Washington* v. *Hume,* 128 U. S. 195, *N. Y. Life Ins. Co.* v. *Deer Lodge,* 231 U. S. 495, and *U. S.* v. *Supplee-Biddle Co.,* 265 U. S. 189, to establish that this Court holds life insurance policies to be contracts of indemnity running from the company to the beneficiary, and (unless payable to the estate) that such policies are no part of the decedent's assets and are not a testamentary disposition of his estate, because the premiums paid in life are neither the policies nor the proceeds thereof (128 U. S. 209).

That those forms of inheritance taxes which can be imposed by Congress *without apportionment,* (1) are

limited to excises, in respect of the *cessation of the decedent's interest by reason of death,* and (2) do not cover the taxation of the *property of others,* even though the death of some one may mark the period of time when such other person may be entitled to alter the form of the property from a chose in action to a collection of its value, is settled by this Court's decisions.

The members of this Court are so familiar with the exhaustive discussions that have taken place at the bar and in consultation over the nature of inheritance taxes, the power to levy them, and the limits of Federal authority in respect thereto that it need only be observed in conclusion:

At last, this Court must decide whether in the Congressional desire to acquire large sums for expenditure, and to inaugurate new social reforms, by a re-distribution of wealth through the confiscation by the State of about half a wealthy man's estate at death, it has not passed the permissible line of action, when it attempts to take an equally large share of what *living* persons have by thrift or otherwise provided as an indemnity against the loss of the family's natural protector by death. Once concede the power of Congress to tax beneficiaries' life insurance, without apportionment it can levy a prohibitive tax on every dollar of the 60 billions in existence, as it matures each year at the rate of nearly a billion a year.

THIRD POINT.

The 25% tax on the life insurance owned by the beneficiaries is void because of the basis on which it is calculated.

If this Court shall extend *Knowlton* v. *Moore* to cover life insurance, nevertheless, this particular Act is void on the following grounds.

1. The Act makes both the executors and the beneficiaries liable for the tax, but as between them, it gives to the executors a right to recover back all, or (depending on the proper construction of the Act) a part of, the tax from the beneficiaries.

Ultimately then, the beneficiaries pay the tax or most of it.

But the tax which the beneficiaries are thus made to pay in respect of the property (insurance proceeds) they own, *is not based in any way upon the property or privileges of the beneficiaries.* It is determined solely by the size of the insured's estate, with which the beneficiaries have, or may have, no concern. If Mrs. Frick and Miss Frick were taxed, at the "estate tax" progressive rates, on the insurance received they would pay about $3,400 and $4,400 respectively—$7,800 in all. But merely because they held insurance on a rich man's life, the tax is $108,657.38.

In short, Congress taxes the beneficiaries not according to any property owned or received by them or privileges exercised, but by the amount of a third person's wealth. Is that taxation at all?

2. Congress has the power to tax—a power that is (so far as we are now concerned) unlimited. It can tax so as to destroy what it taxes. But always it must be in the exercise of the *taxing* power, not the assumed power to redistribute wealth among the people by confiscation. *Loan Association* v. *Topeka,* 20 Wall. 655, at 662-664; Field, *J.,* in the *Pollock case,* 157 U. S. at 599; *Child Labor Tax Case,* 259 U. S. at 38;

Is it within the meaning of "to tax", for Congress to say that A must pay a sum of money, determined not by A's property, expenses, acts, privileges or indeed anything that A receives, does, or has, but solely by what B has? We submit that even the great power of taxation does not cover a *fiat* like that. (For an able discussion see *Coolidge* v. *Nichols,* January 28, 1925, reprinted in Appendix to Mr. Gordon's Brief.)

A somewhat similar situation, though nothing like so flagrant, was presented in *Knowlton* v. *Moore,* but this Court declined to decide the question, because it was able to relieve the injustice by holding that a proper construction of the Act did not require such a result.

But there is no room for construction here, and the question reserved in *Knowlton* v. *Moore* is now presented in an aggravated form. In the *Knowlton* case, the Government contended that the brackets of the progressive inheritance tax rates on legacies were to be determined, not by the amount of each legacy, but by the total estate of the decedent. In rejecting that construction, the Court said:

> "The principle on which such construction rests was thus defended in argument. The tax is on

each separate legacy or distributive share, but the rate is measured by the whole estate. In other words, the construction proceeds upon the assumption that Congress intended to tax the separate legacies, *not by their own value, but by that of a wholly distinct and separate thing.* But this is equivalent to saying that the principle underlying the asserted interpretation is that the house of A, which is only worth one thousand dollars, may be taxed, but that the rate of the tax is to be determined by attributing to A's house the value of B's house, which may be worth a hundredfold the amount. The gross inequalities which must inevitably result from the admission of this theory are readily illustrated. Thus, a person dying, and leaving an estate of $10,500, bequeaths to a hospital $10,000. The rate of tax would be 5%, and the amount of tax $500. Another person dies at the same time, leaves an estate of $1,000,000, and bequeaths $10,000 to the same institution. The rate of tax would be 12½ per cent., and the amount of the tax $1,250. It would thus come to pass that the same person, occupying the same relation, and taking in the same character, two equal sums from two different persons, would pay in the one case more than twice the tax that he would in the other. In the arguments of counsel tables are found which show how inevitable and profound are the inequalities which the construction must produce. Clear as is the demonstration which they make, they only serve to multiply instances afforded by the one example which we have just given. * * *

"It may be doubted by some, aside from express constitutional restrictions, whether the taxation by

Congress of the *property of one person*, accompanied with an arbitrary provision that the rate of tax shall be fixed *with reference to the sum of the property of another*, thus bringing about the profound inequality which we have noticed, would not transcend the limitations arising from those fundamental conceptions of free government which underlie all constitutional systems. On this question, however, in any of its aspects, we do not even intimate an opinion, as no occasion for doing so exists, since, as we understand the law, we are clearly of opinion that it does not sustain the construction which was placed on it by the court below.'"

There might have been some possible excuse for taxing the legacies given by a decedent, at a rate proportioned to the size of his estate; but how can *any* excuse be found for taxing A on *his own* property at a rate determined by *B's* estate?

If this Court holds that the power "to tax", includes the right to tax A on his property, privileges, etc., at a rate determined, not by anything with respect of him, but by something in respect of B (with which A has no concern) then a road has been opened for Congress to avoid every constitutional limitation.

No amount of argument can strengthen the bare statement of the fact that the tax on the beneficiary of the policy is determined by the wealth of the insured. A rich creditor of a poor man, will collect his insurance, free or substantially free of tax; while a poor creditor of a rich man, must pay a 25% tax of the amount col-

lected. Does not the very nature of the phrase "to tax" exclude such a thing?

3. The Government defends the tax by citing cases where an inheritance tax has been sustained, even though the amount of the tax was determined by a percentage of the total estate including therein tax exempt bonds. Where the State permits a decedent to dispose of his estate by will or intestate laws, the State may make a charge for that privilege; and if the charge is a percentage of the estate so disposed of, the incidental fact that the estate may consist in whole or part, of tax exempt bonds, cannot affect the right of the State to charge a tax for the privilege of disposing of the estate. The tax is *not* on the tax exempt bonds *as* bonds. It is on the transfer of the estate and is measured by the size of the estate transferred. The burden on the bonds is merely incidental (*Plummer* v. *Coler*, 178 U. S. 115, 134), and does not prevent the State or Nation from exacting an excise tax in respect of the privilege of transmitting the estate to heirs and legatees instead of escheating to the State.

The judgment should be affirmed.

WM. MARSHALL BULLITT
Amicus curiae.

13 April, 1925.

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